The Business Owners Dilemma

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Maybe you are like the majority of my business owner clients. When I ask them how they feel about their businesses, their answer sounds like this dilemma.

"Hard to live with it, and hard to live without it."

One reason is that every owner pays themselves last. Some people call this The Founder's Trap because no one really understands what it took to create the business and why you had paid everyone else first along the way. Hard to live with it.

Why is hard to live without it? In recent national surveys, 3 out of 4 business owners said they profoundly regretted selling their businesses within a year of getting the big check. Only 5% indicated that they were happy with the financial results. They were the lucky ones, because only about 2 out of every 10 businesses that are put up for sale wind up getting sold, and only 3 in 10 will survive a family transition.

Do you ever think about selling your business or what it might be worth? What about how much would you need to get for your business to maintain the lifestyle you currently have created for yourself? There is nothing more disheartening to a business owner than to learn that all of their years of hard work in building a business and selling it will not allow them to maintain the same lifestyle they have enjoyed while working in the business.

How could this happen? It's known as The Value Gap.

Unfortunately, most business owners have a Value Gap.

The Value Gap is the difference between the current value of a business and what it must sell for so its owner can achieve their desired post-business annual income objective in combination with all their other retirement - oriented assets.

The Problem

Business owners face difficult decisions every day.

Often the decision owners must make to put the business first results in personal and financial sacrifices. Fully funding a 401(k) or IRA plan is usually not the top priority.

For this reason, many owners find that their businesses comprise 80- 90% or more, of the total assets they have available for retirement or their "life after the business."

Business owners, therefore, depend almost entirely upon selling their businesses to fund the income they'll need in their retirement or post-business years.

The value of a business when it is sold can usually be stated as a "multiple" of the cash flow that it generates for its owner.

Cash flow for an owner can take many forms, including salary, benefits, perks, and profit distributions. The value of most businesses is in the range of 3-5 years of expected cash flow, and that's simply not enough capital to fund 20 years or more of annual income like the business currently produces for its owner.

Compounding the issue is that transaction fees, expenses and taxes will further reduce the amount of capital available to the owner post-sale.

Business sellers see the potential sale value of their business as a massive amount of money because it is delivered in a lump sum and the biggest check they've ever received.

What is less understood is the amount of income-producing assets an owner will need to generate a lifetime of income after selling, especially when that income isn't anywhere close to what was being provided through business cash flow.

Can you imagine your “I can’t live without it” scenario. It is usually a nightmare when your life after business income has been dramatically reduced.

The Owner's Trap

The Owner's Trap is identified when a business owner discovers the Value Gap before selling and instead decides to keep going in hopes of growing the business to the point where the Value Gap isn't so monumental. Owners in this situation are actually working harder than ever before, putting in more time than ever, making major capital investments through personal investment and/or borrowed capital, and in the meantime the family is looking on and saying, "When on earth can we ever get off this roller coaster?"

Too many business owners end up in the Owner's Trap, burn themselves out, and waste precious years not enjoying life after business ownership until it's literally too late and they leave the business horizontally. (It sounds a little morbid, but it happens more often than you think.)

There are also too many unfortunate situations where the owner gave the business to the children in exchange for ongoing income as Chairman or other figurehead role only to have the children run the business into the ground after a couple of years and completely destroy the income source their parent is entirely dependent upon.

Concluding Thoughts

For many business owners, the net proceeds from a business sale is not going to come close to replicating the annual income they can extract before selling. Usually 80-90% of the owner's retirement nest egg is connected to the successful sale of their business. Many owners must sell their business for 3-7 times more than current values to have a similar post-sale income for 20+ years. Strategic planning is not usually able to close that gap in value.

If selling a business is going to produce a fraction of the income its owner currently receives, there's a tremendous amount of pressure to get the absolute highest purchase offer possible, and many reasonable offers may therefore be rejected. But what if an owner had a substantial asset completely outside of their business through a preplanned exit strategy; the pressure to hold out and sell for top dollar isn't as great because they have already secured a large source of predictable income. What this means is that an owner can be much more flexible in terms of how they go about selling their business in three ways:

1. They can gift the business to their children and not worry about whether they'll crash the business.

2. They can sell the business at a discount to their managers without worrying that they have no money to pay them up front.

3. They can accept a different deal from a 3rd Party that they might not otherwise be comfortable with, like a lower price, seller financing, etc.

The Preplanned Exit Strategy—Ideal Owner Profile

Not every business owner will qualify. Here are the pre-qualification criteria.

1. Business owner of an established and profitable business.

2. The owner is 45-60 years old.

3. The owner has an exit or transition timeline of between 10 and 15 years.

4. The business has a value (not sales) of between $1 million and $7 million, which translates to net income/earnings in the range of $250,000 to $1,750,000*

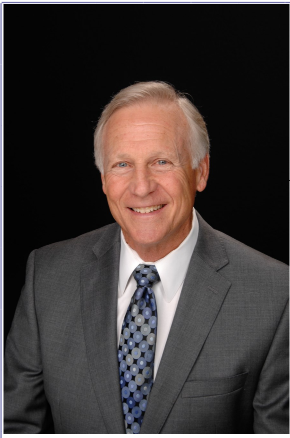
5. The owner has business income of at least $200,000-250,000.

Owners of larger businesses can benefit from the preplanned exit strategy, however, the Value Gap may not be as evident, because the net proceeds will probably be sufficient to maintain their lifestyle. Other planning purposes, such as family estate or wealth transfer planning are also legitimate objectives for these larger businesses.

If you would like to know more about a preplanned exit strategy that might work for you, just call me at my direct line telephone number below, with no obligation of course.

*I will email you an article entitled, "The Owner's Trap" which has a calculator at the end where you can input data and obtain a preliminary business valuation. We think you should know the value of your business, so you can make better decisions about the future of your business and your retirement possibilities.

Knowing the value of your business just might resolve your owners dilemma.



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Ross F. Hoffman is President and Chief Executive Officer of Hoffman & Associates, Estate & Financial Advisors, Inc. He has over 40 years of professional experience in financial, estate, and investment advising. Ross believes everyone should have the opportunity, the freedom and the best information to decide what estate, retirement, and business transition plans work best for them. He has also written articles on these topics.

Ross has earned the most respected professional designations, including Accredited Wealth Management Advisor (AWMA), Accredited Investment Fiduciary (AIF®), Certified Financial Planner (CFP), Chartered Financial Consultant (ChFC), and Chartered Life Under-writer (CLU). He earned his undergraduate degree from UCLA, attended the U.S. Army School of Finance, and the Center of Fiduciary Studies at the University of Pittsburgh.

Ross is an accomplished speaker. He has lectured on Family Wealth Counseling, Evidence Based Investing, Exit Planning, creative uses of life insurance, charitable estate planning to professional groups including the Ventura County Bar Association and the Santa Barbara CPA/Law Society; and has taught estate and gift tax planning.

He is a former co-host of the weekly internet radio show "Conscious Investing," and was in "Navigating the Fog of Investing," a documentary film on the investment industry.

Ross is a prior member of Vistage (formerly TEC), an organization for CEOs, for over 25 years. They presented him the "Widest Range of Knowledge Award" as a Vistage member.

His community involvement has included Vice Chairman and Cabinet member of the Ventura County United Way, Technical Advisory Committee member for the Ventura County Community Foundation, Deferred Giving Board member for the Ventura County Medical Center, Board member of the American Lung Association, Board member of the Ventura County Planned Giving Council, Deferred Giving Committee member for the Boy Scouts of America and a past member of the Estate Planning Council. Ross was on the Board of Segue, a nonprofit, dedicated to keeping kids in school and helping them develop career paths.

Ross's outside interests include golf, daily workouts and time with his family. He also wrote **Back And Better, 37 Rapid Recovery Exercises I Use When Injured or Bedridden**.

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