By: Chuck Goldblum, CFP, CFA
Hurley Capital, LLC
New York, New York

MAXIMIZE YOUR SALE: FROM LOI THROUGH RETIREMENT

You've spent years building more than a business—you've built a culture and a community, a place that created a livelihood and a career for you and your employees. Now you see retirement in the not-too-distant future. Selling your business is a way to realize your legacy and ensure your valued clients are well taken care of.

There are many resources to help you maximize the value of your business and find the right buyer. But is that enough? If you want to maximize the impact of a business sale for your life, there are several steps every business owner/seller can take.

In this article, we will share information and strategies to help you think about how to optimize your personal finances through the sale transaction and beyond:

- MAXIMIZE the after-tax proceeds of the transaction
- PREPARE for your post-deal income/ expense regime
- DEPLOY your sales proceeds to support your retirement, legacy and charitable goals

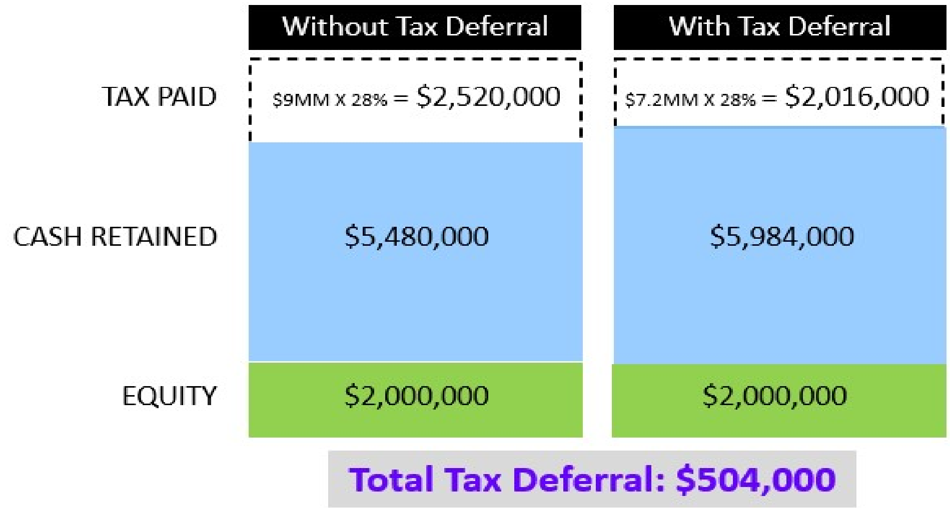
TAX OPTIMIZATION

Tax optimization of your business sale is critical. Saving even a small percentage of taxes on a multi-million-dollar deal translates to a lot of money

There are several tax-optimization strategies that may increase your business sale proceeds: tax deferral on received private-company stock, same-year mitigation and advanced planning. Tax Deferral on Received Stock: In most business sales to private equity-backed firms, sellers receive up to 20% of the deal value in the form of private company stock. While many sellers pay capital gains tax on the entire gain of the sale, the tax associated with the private company stock may be deferred with careful deal structuring. The difference is meaningful, as shown:

In this illustration, the seller receives $10 million for the business and has a $1 million cost basis. Twenty percent of the $10 million is

ASSUMPTIONS	
Sale Price	$10MM
Cost Basis	$1MM (10%)
Capital Gains Tax Rate	28%
Equity Portion	$2MM (20%)



paid in the form of equity of the buying firm. Without a tax deferral on the $2 million of received equity, a seller pays $2.52 million in capital gains tax (20% capital gains tax, plus assumed 8% state income tax), whereas a tax deferral allows the seller to retain an additional $504,000. If the seller lives in a state with income tax, the deferral can be even larger.

As the private-equity shares will likely remain illiquid for years, the seller benefits in two important ways: (1) the seller keeps the cash associated with the tax deferral, and (2) if the shares are eventually sold at a lower value, the seller pays tax only on the lower gain and has no tax-loss carryforward.

Same Year Tax-Mitigation: The income from a sale often causes the owner's highest income year for many years to come. Owners may lower the overall tax rate of a sale by shifting part of the income into future years.

For sellers that typically make annual charitable gifts, sale-year taxes can be reduced through the creation of a donor-advised fund. A DAF works by loading several years of planned charitable donations into a single larger taxable deduction in the year of the business sale. The seller has the added benefit of centralizing donations and eliminating receipt tracking. A DAF streamlines the charitable-gift process while providing an upfront tax benefit.

Another way to defer same-year taxes is through the use of Opportunity Zone investments or installment-sale transactions. An Opportunity Zone investment is a business or real estate development with specific federal government tax incentives. Sale profits reinvested in an Opportunity Zone are not liable for capital gains taxes until the 2026 tax year. Furthermore, if the Opportunity Zone investment is held for over 10 years, there are no capital gains on the sale, ever. Installment sales are deal structures that pay sellers over several years, allowing for capital gains to be spread out. Some sellers prefer to avoid installment sales as sales proceeds and reinvestment opportunities are delayed until the monies are received.

Advanced Planning: For owners not selling for a year or more, there are two inter-related advanced planning strategies that may work—one for mitigating taxes in some high-tax states and one for estate planning purposes.

In both cases, the owner sells the business at a discounted/appraised valuation to an irrevocable trust (or trusts) domiciled in a no-income-tax state. If the trust is structured as a grantor trust, where the owner is liable for taxes on income in the trust, no tax will be due on this transaction. When the business is then sold to the outside buyer, taxes are due based on the location of the trust.

This structure is also useful for estate planning if the owner has a large estate, regardless of state income tax, as the trust/s will (1) capture the entire value between the discounted sale from the owner and the sale to the outside buyer, and (2) the owner is liable for paying all of the capital-gains taxes. For large estates, this can be a very valuable technique. We suggest consulting a tax lawyer to get the best advice for your situation.

POST-DEAL INCOME AND EXPENSES

With a business sale, an owner exchanges income and expense flexibility for a fixed, lower salary with a possible earn-out. Expenses such as car payments, insurance and wireless services may no longer be paid for by the business and are now the seller's personal responsibility. This new fixed salary may not cover increased living expenses; dipping into savings may be required. This transition can be unnerving to many, as successful business owners are accustomed to adding to their savings on a continual basis.

The solution is to create a plan that works from the salaried work years through retirement.

Ask the following questions:

- What is my new income?
- What type of earn-out am I receiving? What's the likelihood of achieving it?
- Am I retiring after this employment contract expires?
- Do I own the office that my business occupies? If I'm renting the office to the new owner, what do I make from the rent? Will I sell the office afterwards or rent it further? For how much?
- What other income do I expect, such as Social Security and IRA distributions?
- What are my current living expenses?
- Are there other one-time expenses to consider, such as children's weddings, education or a planned relocation?

All this information helps to project and protect future finances. The important takeaways are::

1. The answers to the questions above are the beginning of a good financial plan. As facts change, plans can be adjusted as well.
2. The results may be surprising. Maybe that vacation home is doable!

3. Armed with detailed financial facts, business-sale proceeds can be deployed in the most beneficial way.

DEPLOYING YOUR SALES PROCEEDS

A business owner's personal finances are usually dominated by his/her business holdings. With a sales transaction, the proceeds, along with the dissolution of the company retirement plan, create an unprecedented amount of liquidity and some big decisions:

- Do I need any of the sales proceeds on an annual basis to support my lifestyle?
- Can I afford to live off the gains on my investments or will I need more?
- What sort of investment return do I need?
- Do I have specific plans to allocate funds to charity or to my beneficiaries?

With this information, an efficient investment plan can be created. This plan can include stocks, bonds, real estate and even a new business venture. The key is knowing the return you need on your investments and taking the steps to achieve that goal. With new investments come new opportunities for tax optimization, such as prioritizing dividend income or real-estate income, or timing Social Security withdrawals or Roth conversions of your IRA.

A business sale is a liberating moment— as well as a huge accomplishment for many owners. The dollar amounts involved are large and the benefits of getting the details right can make a profound difference in maximizing sale proceeds. With a little foresight, specific solutions are available and achievable. The goal is to feel comfortable with the decisions you've made. The right research and planning can empower even the most seasoned business owner as you execute what may be the most important transaction of your career.

Chuck Goldblum is the founder of Hurley Capital LLC. He advises benefits brokerage owners and sellers on tax planning, financial planning, budgeting, investing and private company stock. His ability to provide strategic personal financial direction has benefitted agency owners across the country. Out of the office, Chuck enjoys exploring NYC with his wife and three girls, as well as running and skiing.