PARTICIPANT GUIDE

FDIC Money Smart

Financial
Education Curriculum

SBA

Selling a Small Business and Succession Planning for a Small Business

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Welcome

Welcome to the *Selling a Small Business and Succession Planning for a Small Business* module. By taking this training, you are taking an important step to building a better business. This guide accompanies the *Selling a Small Business and Succession Planning for a Small Business PowerPoint Presentation*.

Objectives

After completing this module, you will be able to:

- Explain how to change the ownership of a business through selling, closing, or handing the business to successors.
- Explain how to establish an exit strategy for retirement which includes a succession plan, transferring ownership of the business, and paying taxes.

What Do You Know? Selling a Small Business and Succession Planning

Instructor: ________________________________ Date: ____________________

This form will allow you and your instructors to see what you know about selling a small business and succession planning, both before and after the training. Please read each statement below. Circle the number that shows how much you agree with each statement.

	Before Training				**After** Training			
	Strongly Disagree	**Disagree**	**Agree**	**Strongly Agree**	**Strongly Disagree**	**Disagree**	**Agree**	**Strongly Agree**
1. I can explain how to change the ownership of a business through selling, closing, or handing the business to successors.	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**
2. I can explain how to establish the right exit strategy for retirement which includes a succession plan, transferring ownership of the business, and paying taxes.	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**

Pre-Test

Test your knowledge of selling a small business and succession planning before going through the course.

1. **Which of the following are reasons to sell your business? Select all that apply.**
   a. New job offer
   b. Profits are more than needs
   c. Market or industry changes
   d. Someone offers to buy
   e. Ready to retire

2. **Most business valuation methods are a combination of two factors: ________________________.**
   a. Revenue stream and assets
   b. Customer base and net worth
   c. Gross profit and assets
   d. Revenue stream and net worth

3. **When selling your business it is important to know both the buyer's financial ability and the buyer's management skills.**
   a. True
   b. False

4. **Succession planning deals with the process of ________________________.**
   a. Determining a plan for your business over the next five years
   b. Identifying buyers for your business
   c. Passing control of your business to others
   d. Selling your business to family members

5. **Small business retirement plans are not recognized by the Internal Revenue Service (IRS).**
   a. True
   b. False

Determining If a Business Should Be Sold

While many businesses run for years, even over several generations, businesses open and close all the time. Here are a few reasons why you may want to sell or close your business.

Business or professional reasons include:

- Job offer from another company
- Purchase offer for your business or your business assets
- Dissatisfaction with sales and profits
- Changes in the market or industry

Personal reasons include:

- Retirement
- Burnout with self-employment
- Health concerns or family needs
- Desire to go in a new direction

Discussion Point #1 Reason for Selling the Business

The purpose of this question is to discuss your reasons for selling the business with the class participants.

What is the main reason for selling your business?
____
____
____

Selling a Business

If you decide to sell your business, here are factors to weigh.

Determine If Business Is Saleable

Before starting, you need to determine if you have a saleable business. Here are some questions to consider when determining if you have a saleable business.

Do you have a history of strong profits?
A financially strong business has a lot to offer a new owner. If your business is struggling financially, the business will not be as attractive to buyers. Sometimes a business does not

even have a market value beyond the assets of the business.

Is the business in an attractive industry?
Some types of businesses have more appeal than others.

Is the business in a location convenient to potential buyers?
Location is important to many businesses. Some businesses can be easily moved, others cannot.

Are your assets in good shape?
Having assets in good condition, with significant market value and remaining useful life, adds to your business' value.

Do you have quality inventory and good supplier relationships?
A prospective buyer wants to see quality (e.g. fresh) inventory and solid relationships with suppliers.

Do you have a solid customer base?
A healthy list of returning customers makes your business more valuable and attractive.

Can you transfer your business to another person?
Some businesses are dependent on a particular person's talents and cannot be transferred to another person.

Do you have a healthy balance sheet?
A combination of good retained earnings and net worth, low debt, and collectable accounts receivable make for an attractive business that is worth purchasing.

Determine Your Price

The value of your business can be determined by many business valuation methods. Most valuations are a combination of two factors:

- Assets, such as cash, receivables, inventory, equipment, and real estate
- Revenue stream, that is, net profit over time

Assets are usually priced using market valuation. Valuing revenue stream is more complicated, involving return on investment, comparisons to alternative investments, and growth potential.

Many owners get help from accountants, attorneys, and industry specialists when determining the value of their businesses.

Prepare for Sale

When preparing for the sale, here are some items to consider:

- Resolve outstanding issues such as unpaid accounts receivable, debt, lawsuits, and environmental hazards.
- Demonstrate that accounts receivable can be collected.

- Prepare historical and projected financial statements.
- Provide a convincing business plan for the future.
- Secure beneficial relationships with suppliers and customers.
- Get the premises in good shape.
- Sell old inventory.

In addition, you must determine exactly what equipment is included in the sales price and make sure all this business and office equipment is in good order. Finally, you should provide a clear picture of how you will be compensated as the owner.

Look for Prospective Buyers

Prospective buyers may include:

- Employees with enough management experience and skill to take over the business
- Long-standing customers who might have a passion for your product or service
- Business owners whose businesses would be enhanced by your product or service
- Competitors who might see a benefit in absorbing your business

You will want to advertise online, through trade associations, and via email to inform potential buyers that your business is for sale.

Negotiate the Deal

Negotiating and structuring a business sale is a complex process. Many business owners engage the expertise of attorneys and accountants. Here are some of the issues to consider.

Buyer qualification
Just like buying a home, buyers need to demonstrate the financial ability to purchase a business. Demonstrated financial ability includes having sufficient cash and the credit worthiness for borrowing part of the purchase price. A prospective buyer should also demonstrate the management skills to run the business.

Payment in lump sum or installments
Buyers can provide the entire price, through a combination of cash and loans from banks, or pay the business seller in installments.

Non-compete agreement
Often business sellers are required to sign an agreement to not start a competing business for a few years.

Management assistance
The new owner of a business may benefit from the previous owner's expertise. The seller of a business often will serve as a paid consultant or manager for a few months to help the new owners learn how the business operates.

Sales agreement preparation

A sales agreement covers many elements of the sale including sale price, buyer deposit, promissory note, security, seller and buyer's representations, contingencies, dispute resolution, and more.

Down payment

If a purchase is to be paid in installments, the buyer and seller must agree on a down payment.

Collateral

If the purchase requires a loan, all parties must agree on collateral. Often the business itself is collateral. However, if the seller does not want the business back in the case of a default, the parties can negotiate a different form of collateral.

As you can see, many factors are involved in the sale of a business. You should work with an experienced attorney and an accountant to help structure the deal and prepare all the documentation.

Discussion Point #2 Challenges of Selling the Business

The purpose of this next question is to discuss some of your concerns about selling the business with other participants.

What are some of the challenges of selling your business?
____
____
____

Closing a Business

Here are a few reasons why it might make more sense to close a business rather than sell it:

- The businesses might be too small, with insufficient assets and profitability, to interest a buyer.
- Businesses in decline are not promising investments.
- Businesses that are specialized, located in remote areas, or have other unique characteristics may be difficult to sell.
- Businesses with significant assets, but not sales, might be better off selling the assets and closing.

Here are some steps to take when closing your business.

Follow Instructions in Your Founding Documents

If you're a sole proprietor, you don't need to worry about closing according to the requirements of business organizational documents. If your business is a general partnership that doesn't have a written partnership agreement, then you need to give notice to your partner of your express desire to withdraw from the partnership. On the other hand, if your business is a partnership with a written partnership agreement, a limited liability company (LLC), or a corporation, you will need to follow the rules of dissolution contained in the partnership agreement, articles of incorporation, or applicable state laws.

File Dissolution Documents with the State

All limited and general partnerships that filed with a state at the inception of the partnership must file dissolution papers with the state. Once you have voted to dissolve an LLC or corporation, you file paperwork with the state, certifying the decision to terminate the business. Filing a certificate of dissolution (also known as articles of dissolution) is a process that varies from state to state.

Sell Business Assets

If you have business assets, equipment, inventory, and real estate, you will likely want to sell your assets before closing the business.

Cancel Permits, Licenses, and Lease Agreements

Review all the registrations, licenses, and permits you obtained to open and run your business. Contact licensing and permitting agencies and follow their cancelation processes. If you are leasing office space or equipment, you will need to terminate your leases—review your lease agreement for the details, including what penalties you may incur.

Comply with Tax Laws

When you end a business, the company is still liable for taxes in the prior and the current year. This means that you must continue making deductions from paychecks and continue payroll reporting obligations. You should continue to file your quarterly or annual taxes, and your capital gains and liquidation forms. You will also be responsible for all final tax forms that need to be filed, including forms for income tax, sales tax (that has been collected), and payroll taxes.

Resolve Outstanding Issues with Customers, Creditors, and Suppliers

Pay all of your debts, collect balances due from customers (receivables), and close all of your accounts.

Maintain Records

Although you’ve closed the doors, continue to maintain and retain business records. You will need to file income taxes, answer inquiries, and respond to agencies seeking information. You could still be audited and may need to answer questions from those with whom you have done business.

Get Help

Seek help from your accountant and attorney to review the closing process.

Planning Succession

Succession planning involves creating a plan for someone to either own or run your business after you retire, become disabled, or die. In simple terms, succession planning is the process of passing control of the business to others. Here are some steps to take for succession planning.

Find Successor

If you are passing the business to a family member, you may consider transferring ownership through your estate planning process. Often, however, new management comes from your pool of existing employees. If you have a larger business (such as an LLC or a corporation), succession planning involves preparing people for management and leadership roles in order to replace you or other managers when the time arises.

Finding your replacement is difficult so plan ahead, it is best to start early. Leaders are not always easy to find and it takes time to mentor someone into a management role. You will need to identify potential successors in your family or among employees. You can hire from outside the company, but it's helpful to groom someone already in your business, over a period of time, so the transition to new leadership will be smooth.

Train Successor

Once you have successors identified, deliberately create a training plan to ensure that everyone involved has time to learn the skills, gather the information, and practice the leadership roles critical to the future success of the business.

Whether you are transferring a business to a family member or you are promoting employees into leadership roles, you need to plan ahead. A succession plan takes into consideration the development of future leaders' skills and abilities. The plan should deliver a return on your business's training investment by providing for your successors' advancement while simultaneously ensuring your successors don't leave your business. Even if someone leaves, a current employee should be ready to step into the vacated role. As the need arises, with good succession planning, employees or family members are ready for new leadership roles.

Ease Tax Exposure

Tax exposure arises when one generation gives way to the next generation in a closely-held family business. In this case, succession planning and estate planning become intertwined by the family. Multiple types of taxes must be considered when planning this type of succession, including:

- Income tax
- Gift tax
- Generation-skipping tax
- Estate tax

Start family succession planning sooner, rather than later, because starting sooner will give you more flexibility with your planning. Consult an attorney and an accountant about putting the proper estate documents in place, especially for succession planning in a family business.

Discussion Point #3 Benefits of Selecting a Successor

The purpose of this discussion is to provide reasons for selecting a successor.

What is the most important reason for selecting a successor?
____
____
____

Planning Retirement

Small business retirement plans are a means to help employers and employees save toward retirement.

Retirement Plan Benefits

A retirement plan has many benefits. Primarily, a retirement plan helps you and your employees to save and invest toward financial security in retirement. You and your employees get significant tax advantages and other incentives:

- Employer contributions are tax-deductible.
- Assets in the plan grow tax-free.
- Flexible plan options are available.
- A retirement plan can attract and retain employees, reducing new employee training costs.

Employee benefits include:

- Contributions to the plan reduce current taxable income.
- Contributions and investment gains are not taxed until the contributions and gains are distributed.
- Contributions can be easy to make through payroll deductions.
- Small regular contributions can grow to significant retirement savings over time as a result of compounding. The earlier in life an employee starts to save, the more they will benefit from compound growth.
- Retirement assets can be transferred to a new plan if the employee leaves the company.

Retirement Plans

The Internal Revenue Service (IRS) recognizes small business retirement plans as a means to help employers and employees save toward retirement. People tend to think of an IRA as something that individuals establish on their own, but an employer can help its employees set up and fund their IRAs. With an IRA, the amount that an individual receives at retirement depends on the funding of the IRA and the earnings (or losses) on those funds. The plans are relatively easy to establish--your financial institution handles most of the details. There are three key types of IRA-based options:

- **Simplified Employee Pension Plan (SEP):** Simplified Employee Pension (SEP) plans are available for any size business. Only the employer contributes to the retirement plan—the employer can contribute up to 25 percent of each employee's pay. The contributions are made to a traditional IRA. Contributions to a SEP are tax deductible and your business pays no taxes on the earnings on the investments. You may be eligible for a tax credit of up to $500 per year for each of the first 3 years for the cost of starting the plan.

- **SIMPLE (Savings Incentive Match Plan for Employees) Individual Retirement Account Plan:** A SIMPLE IRA plan allows a business that has 100 or fewer employees to help employees save for retirement. Employees can contribute to the IRA, on a tax-deferred basis, through payroll deductions. As the business owner, you can choose either to match the employee's contributions or to contribute a fixed percentage of all eligible employees' pay. You may be eligible for a tax credit of up to $500 per year for each of the first 3 years for the cost of starting a SIMPLE IRA plan.

- **Payroll Deduction IRAs:** Even if an employer does not want to adopt a retirement plan, it can allow its employees to contribute to an IRA through payroll deductions. The employer sets up the payroll deduction IRA program with a bank, insurance company or other financial institution, and then the employees choose whether and how much they want deducted from their paychecks and deposited into the IRA. Employees may also have a choice of investments depending on the IRA provider. The employee makes all of the contributions. There are no employer contributions.

Under Federal law, individuals saving in a traditional IRA may be able to receive some tax advantages on the money they save, up to a certain amount, and the investments can grow tax-deferred. If the individual selects a Roth IRA, the employee's contributions are after-tax and the investments grow tax-free. A Roth IRA, like the Traditional IRA, provides for retirement withdrawals after the age of 59 ½ (within the guidelines). However, the tax benefit is opposite from the Traditional IRA. Whereas the Traditional IRA allows for a tax deduction in the year for which the deposit was made, the Roth does not. The benefit of the Roth IRA is that no tax is levied on the interest income after you retire.

Another retirement plan option is **defined contribution** plans, such as a 401(k) plan or a profit-sharing plan. These employer-established plans also do not promise a specific amount of benefit at retirement. Instead, employees or their employer (or both) contribute to employees' individual accounts under the plan, sometimes at a set rate (such as 5 percent of salary annually). At retirement, an employee receives the accumulated contributions plus earnings (or minus losses) on the invested contributions. Defined benefit plans, on the other hand, promise a specified benefit at retirement, for example, $1,000 a month at retirement.

A common defined contribution plan option is the **401(k) Plan.** A 401(k) plan allows participants to decide how much to contribute to their accounts, and employers are entitled to a tax deduction for any contributions they make to employees' accounts. The money contributed may grow through investments in stocks, bonds, mutual funds, money market funds, savings accounts, and other investment vehicles. Contributions and earnings generally are not taxed by the Federal Government or by most State governments until they are distributed. 401(k) plans can vary significantly in their complexity. However, many financial institutions and other organizations offer prototype 401(k) plans, which can greatly lessen the administrative burden on individual employers or self-employed individuals of establishing and maintaining these plans. Banks that provide 401(k) retirement savings products will generally assist you in setting them up with your employees and even provide education for your employees on important features of the plan.

Starting a Retirement Plan

Starting a retirement savings plan can be easier than most business owners think. By starting a retirement savings plan, you will help your employees save for the future. What's more, retirement programs can provide tax advantages to both employers and employees. You can establish a plan even if you are self-employed.

Review retirement plans with a tax advisor. Then, as necessary, contact a plan administrator to open your small business retirement plan. Ask your bank, accountant, or business attorney for plan administrator recommendations.

If you have employees, notify them about the plan, including the plan's provisions and eligibility guidelines. Eligibility guidelines should include an enrollment period when administrators are available to answer employee questions.

When the plan is in place, integrate contributions to the plan into your regular business and financial management practices. Retirement savings should be built into your overall business plan to ensure there are sufficient profits to provide for retirement savings.

Top Three Key Points to Remember

1. Transitions that include selling a business, closing a business, and retiring are all part of the life cycle of a business, and you should prepare for them.
2. If you are just starting your business, you may not need to focus on all of these transitions right away.
3. However, you should have a strategy to save for your retirement and work toward it with regular contributions to your retirement account. Small business retirement plans are a means to help employers and employees save toward retirement.

For Further Information

Federal Deposit Insurance Corporation (FDIC)
www.fdic.gov
The Federal Deposit Insurance Corporation (FDIC) preserves and promotes public confidence in the U.S. financial system by insuring deposits in banks and thrift institutions for at least $250,000; by identifying, monitoring, and addressing risks to the deposit insurance funds; and by limiting the effect on the economy and the financial system when a bank or thrift institution fails.

The FDIC encourages bank lending to creditworthy small businesses. The FDIC also encourages small businesses that may have an inquiry or concern about the availability of credit to contact the FDIC Small Business Hotline at 1-855-FDIC-BIZ or www.fdic.gov/smallbusiness. Another FDIC website, www.fdic.gov/buying/goods, provides resources to assist small businesses that may want to do business with the FDIC.

U.S. Small Business Administration (SBA)
www.sba.gov
SBA Answer Desk: 1-800-827-5722
The U.S. Small Business Administration (SBA) web site provides resources, answers to frequently asked questions, and other significant information for small business owners.

U.S. Financial Literacy and Education Commission
www.mymoney.gov
1-888-My-Money (696-6639)
MyMoney.gov is the federal government's one-stop web site that provides financial education resources from more than 20 federal agencies.

Post-Test

Now that you've gone through this module, see what you've learned.

1. **Which of the following are reasons to sell your business? Select all that apply.**
   a. New job offer
   b. Profits are more than needs
   c. Market or industry changes
   d. Someone offers to buy
   e. Ready to retire

2. **Most business valuation methods are a combination of two factors: ________________________.**
   a. Revenue stream and assets
   b. Customer base and net worth
   c. Gross profit and assets
   d. Revenue stream and net worth

3. **When selling your business it is important to know both the buyer's financial ability and the buyer's management skills.**
   a. True
   b. False

4. **Succession planning deals with the process of ________________________.**
   a. Determining a plan for your business over the next five years
   b. Identifying buyers for your business
   c. Passing control of your business to others
   d. Selling your business to family members

5. **Small business retirement plans are not recognized by the Internal Revenue Service (IRS).**
   a. True
   b. False

Evaluation Form

Your feedback is important. Please fill out this evaluation on the *Selling a Small Business and Succession Planning for a Small Business* training.

Module Rating

1. Overall, I felt the module was (check one):

 [ ] Excellent

 [ ] Very Good

 [ ] Good

 [ ] Fair

 [ ] Poor

Please indicate the degree to which you agree by circling a number.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
2. I achieved the training objectives.	1	2	3	4	5
3. The instructions were clear and easy to follow.	1	2	3	4	5
4. The PowerPoint slides were clear.	1	2	3	4	5
5. The PowerPoint slides enhanced my learning.	1	2	3	4	5
6. The time allocation was correct for this training.	1	2	3	4	5
7. The instructor was knowledgeable and well-prepared.	1	2	3	4	5
8. The participants had ample opportunity to exchange experiences and ideas.	1	2	3	4	5

Please indicate the degree of knowledge/skill by circling a number.

	None				Advanced
9. My knowledge/skill level of the subject matter **before taking the training**.	1	2	3	4	5
10. My knowledge/skill level of the subject matter **upon completion of the training**.	1	2	3	4	5

Instructor Rating

11. Instructor Name:

Please use the response scale to rate your instructor by circling a number.

	Poor	Fair	Good	Very Good	Excellent
12. Made the subject understandable	1	2	3	4	5
13. Encouraged questions	1	2	3	4	5
14. Provided technical knowledge					

15. What was the most useful part of the training?

___

___

___

16. What was the least useful part of the training and how could it be improved?

___

___

___