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Boomers Bailing from Businesses

There's much being said about advising those undersaving boomers, but how about boomers who have built successful businesses?

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By DAVID J. DRUCKER

Boomers are hotter than Georgia asphalt these days. The industry has awakened to the fact that these quirky 42-to-60-year olds are going to be everyone's retirement-aged clients in just a few short years — their parents' generation either gone or ensconced in assisted living centers making very few decisions without the help of their boomer children.

Of course, the common characterization of boomers is that they're spendthrift so-and-so's, unprepared for retirement, destined to crash and burn. Less publicized is the fact that many have accumulated significant equity in homes and businesses and, along with inheritances from parents dying mercifully un-prolonged deaths, will actually be just fine... that is, if they have the right guidance when it's time to sell their businesses.

We asked experienced advisors the most important considerations and strategies to weigh when advising boomer business-folk on converting businesses into income streams. Four themes came up over and over again: valuation, teams, taxes and the softer side — what they will do when they're no longer down on the farm.

Valuation

Says David Lewis, president of Resource Advisory Services in Knoxville, Tenn.: "The trick will be to optimize business valuations." In many industries, rules of thumb develop that don't match reality and don't provide reliable guidance to sellers. "In our own industry," says Lewis, "we've seen the 'two-times-revenue' rule of thumb and locked in on that without questioning it through rigorous business appraisals. And, in my experience with clients selling businesses over the years, I virtually always see vast differences between the values they place on the businesses at the beginning and the values they receive when they actually sell."

One of the best things we can do, says Lewis, is find ways to help boomers get a realistic understanding of the true values of their businesses. Adds Michael Potito of Singer Potito Associates in Amherst, Mass., many businesses, especially professional

businesses, don't have a "natural income stream." They may have a client list that's worth something, but if the business owner must initiate the sale of services to the client, the list may not be all that valuable. "The doctor with his own medical practice doesn't call up his patients and say, 'Hey, are you sick yet because we're offering a good deal today.' Businesses with an income stream that transcends the originators will have a lot of value."

Look for a professional to assist in the valuation process — someone with an AVA designation. "This stands for Accredited Valuation Analyst, which is a specialty in valuing small businesses," says Potito, who himself carries the designation. Of course, a CPA with a Certified Valuation Analyst designation is also a good choice.

Teams

In addition to a valuation specialist, your team (assuming you don't possess some or all of this training yourself) should include a CPA, business attorney, and possibly an actuary, says David Morganstern of CMC Advisers, LLC in Portland, Ore.

"The CPA is a critical advisor for apportioning the sale price to either assets or stock for capital gains purposes. The business attorney is instrumental in negotiating the business transfer and reviewing the contract between the buyer and seller. And we have consulted with an actuary when the sale would impact a defined benefit plan already in force wherein the business owner would have a liability to employees."

A team should also include a financial planner and an insurance specialist, says **Gregory Banner of Asset Preservation Strategies in San Diego**. As an advisor specializing in exit planning, Banner says no one advisor will have all the necessary skills required for proper exit planning. In addition to structuring the team with all the right advisors, he adds that all team members must be able to "check their egos at the door" and collaborate with the client's best interest in mind.

Taxes

Business sales inevitably throw off taxable income and/or capital gains, and there are plenty of creative ways to reduce or delay both. In the sale of my own book of business from my C-corp advisory firm in 2001, I learned that I could take capital gain treatment on my personal return for the goodwill inherent in my client relationships (precedents: *Martin Ice Cream Co. v. Commissioner of Internal Revenue*, 1998, and *William Norwalk v. Commissioner of Internal Revenue*, 1998).

Martin Shenkman, a tax attorney in Teaneck, N.J., suggests counseling the client to consider a time-honored technique used in many capital gain situations — the charitable trust coupled with an insurance trust. Says Shenkman: "One strategy is to gift part of the business interests to a charitable remainder trust (CRT) before the sale. The boomer client gets a charitable contribution deduction to offset some of the gain on sale and the CRT provides cash flow during retirement." He adds that an insurance trust can

be used to replace the portion of the business gifted to the CRT. "Some planners call this a 'wealth replacement trust,' but it's really a standard insurance trust."

Of course, it's important to leave a piece of the sale unencumbered by planning so the boomer can have free reign of the money.

The Softer Side

Good business planning touches more than just technical considerations. "The first issue we address with those exiting businesses is what will the boomer do next," says Ron Rhoades, director of research with Joseph Capital Management of Hernando, Fla.

"This is by far the hardest issue for entrepreneurial-minded boomers to face. Surprisingly few of them plan for what they will do in retirement." Rhoades asks his client-sellers a series of probing questions about their interests and goals — or lack thereof. "We often get [insightful] answers when asking them to describe a typical week during retirement." Some boomers, says Rhoades, will do better in retirement if they take jobs in the field in which they worked previously — but for 40 or fewer hours a week, not the 50 to 65 hours they endured as business owners.

The key to a successful retirement, says Rhoades, is having the proper mindset. "It's a huge psychological challenge to go from paying bills with a paycheck to paying them from a retirement nest egg." Undertaking projections of withdrawal rates helps, says Rhoades, as do projections of living expenses and taxes based upon checkbook ledgers and credit card bills for the past 12 months. In other words, it's one thing to negotiate a business sale, but quite another to convince the client his business proceeds are going to take care of him for the rest of his life.

We've all heard the saying, "It's important to know what you don't know," and this couldn't be truer than in the case of a client with a business to sell. Unless you have a background in business brokerage, it's unlikely you'll be expert at business valuation, contracts, negotiating, taxation, actuarial considerations and counseling the client through this major life change. Know your shortfalls and bring in the right people. Doing so will keep you in charge of your client, not to mention the proceeds of his business sale.

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