



October 2011

Transition Planning Case Study – Part II of III

This second newsletter in a series of transition planning cases (you can find 'Part I' on our website in the 'Events' tab under the topic of transition & exit strategies) is intended to further put into action many of the multi-layered and theoretical aspects of transition planning. It is intended to have you begin to see yourself in the position of our transitioning owner, Bill Brown, to see how much of our transition planning system can apply to your situation.

When we last left off, Bill Brown had recognized the value of planning for his transition and was following the direction of his transition planning advisor, Tom. Tom is having Bill follow a system for his transition and he has gone through one of the most challenging of the 6-step process – the first step of establishing goals and envisioning a life beyond Bill's business. Bill sees that these exercises are putting him in a position of moving closer and closer to a transition and are helping Bill to make better decisions in his business to provide for this transition in the future.

Step #2 – Bill's Readiness for His Transition

After setting his goals, Tom is now helping Bill to measure and better understand his personal readiness for his transition. There are two (2) primary components to measuring an owner's readiness for their transition. The first is the 'financial readiness' of the owner and next is the 'mental readiness.' We begin with Bill's Financial Readiness.

Bill's Financial Readiness for His Transition

Tom knows that Bill is going to need specific guidance as to whether or not he can afford his transition. The reality of most business owners is that they spend

much more than their W-2 income within their business. This means that most owners of private businesses live out of their businesses' by personally expensing many items. Beyond this issue there is also the fact that owners tend to have most of their wealth concentrated into their businesses, constantly betting on themselves and their company's potential for growth.

After twenty (20) years of building his brewery business, Bill, like most owners, has most of his wealth tied to his illiquid business. Also like most owners, Bill has a relatively small amount of money saved outside of his business. This means that Bill's Financial Readiness is 'Low.' With a Low financial readiness, Tom needs to provide specific guidance to Bill as to how he can turn his illiquid business wealth into cash or a stream of tax-efficient income that Bill can have access to in order to provide for his post-transition lifestyle.

In our example, Bill has \$800,000 saved in his investment accounts but spends almost \$280,000 in after-tax expenses every year. This means that at 58 years old, Bill only has a few years of living expenses available to accommodate his annual lifestyle. The difference between what Bill has saved and what he needs is his Value Gap. Tom determines that Bill will need to get a significant amount of his illiquid business wealth out of the business to pay for his post-transition lifestyle.

Mental Readiness for Bill's Transition

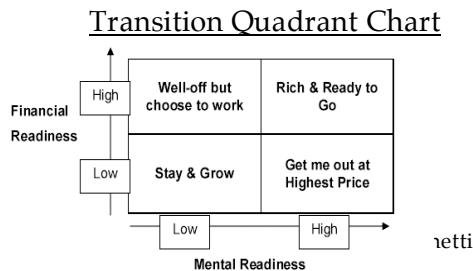
Mental readiness, generally, is an owner's willingness to stop working. In our last newsletter Bill commented to Tom that he is not ready to 'let go' of the business. Accordingly, Tom and Bill are planning on a long range transition for Bill from his

business. Bill recognizes that a transition plan does not mean that he is leaving the business anytime soon or that he is going to necessarily sell the business to someone else. In fact, with a Low Mental Readiness, Bill can focus on removing himself from the business over a longer period of time, keeping his job and maintaining control over his business and eventual transition.

Bill’s Mental Readiness can also be equated to his time frame for a transition. In this case Bill wants to understand how he can remove the equity in his business while also continuing to work over a number of years.

Step #3 – Type of Transitioning Owner

In our third step of the transition planning process, Bill wants to understand what type of transitioning owner he most resembles. In this case Tom helps Bill see that based upon his Financial and Mental Readiness, Bill most resembles a ‘stay and grow’ transitioning owner. The Transition Quadrant Chart below illustrates this important point.



Bill is in agreement with Tom’s assessment but now wants to know how he applies this to his transition planning.

Step #4 – Transition Options

Our fourth step in the transition planning process is helping Bill understand the options that are available for his transition. As we saw, Bill is interested in options that are aligned with his personal readiness. Once Bill comes to understand his various options for transition, he will be in a position to choose the direction that he wants for his transition. The five (5) primary transition options that Bill can pursue are:

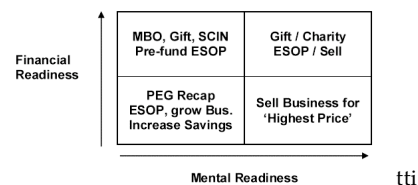
1. Sale of the Business

2. Private Equity Group Recapitalization
3. Employee Stock Ownership Plan (ESOP)
4. Management Buyout
5. Gifting

Transition Option Chart

These options for Bill’s transition are put into the Transition Options Chart below so that Bill can begin to understand the options that are most applicable to his current readiness for his transition.

Transition Options Chart



This fourth step in the 6-step transition planning process is designed to have Bill understand that there are many ways to transition a business. The option that is best for him will be the one that moves him in a definite direction towards a successful transition.

Tom has helped Bill measure his goals and his readiness for his transition. Bill has come to understand how the different options for a transition apply to his situation and how the 6-step transition planning process is most helpful in moving Bill’s thinking toward confidently transitioning his business and protecting his illiquid wealth.

Since the first conversation with Tom, Bill has come a long way in his thinking about his transition, now better understanding the proven 6-step system for a transition and how it can help him define and achieve success for his transition.

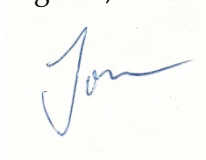
What remains now is Bill’s ability to get enough value to meet his financial needs and then to make certain that he does not lose it to taxes and other wealth detractors. That will be the focus of our next and final newsletter for this case study.

If you have found this case study has raised questions you would like to discuss or inspired you to find out how a comprehensive transition strategy can fit your situation, you are always welcome to come to one of our Executive Briefing to learn how our process works, or contact Owner's Edge to discuss how transition planning will help you.

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Regards,

A handwritten signature in blue ink, appearing to read "Tom", is placed on a small, light-colored rectangular background.

Our Commitment to our Customers

We help our owner/clients articulate and execute the strategies needed to make their profits sustainable and their business transferable. This creates true and meaningful value.

About Owner's Edge

Owner's Edge is a business advisory and consulting firm specializing in helping business owners work *on* their businesses by devising and implementing strategies to drive operational excellence every day. We are one of the few advisor firms that can provide a formal and comprehensive Transition Planning service for business owners. Call us for a no-obligation consultation today.

Executive Briefing: *Business Transition Strategy Planning*

Wednesday November 2, 8:00AM – 10:00AM
Hope Club, Providence

This educational breakfast briefing is tailored especially for business owners and their key advisors. Learn why it is important to plan your transition, where you should start, what your transition options are, who is involved in the process and when they need to enter into the process. A continental breakfast will be served. Reserve your seat today and feel free to invite members of your advisory team.

Host & Speaker: Tom Stocker, Managing Director, Owner's Edge

Investment \$25.00

Kindly RSVP by October 31, 2011
to Lauren McCarthy, Newberry PR & Marketing,
401-433-5965 or lauren@newberrypr.com.

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