Why Do I Need A Financial Roadmap If I Am Selling My Business?

PagnatoKarp
Transparent Family Wealth Advisors

Financial independence can be defined as working because you want to, not because you have to. But how much wealth do you require before you have achieved financial independence? At what point are you able to sell your business with complete confidence that your current lifestyle can be maintained?

IT'S ABOUT HOLISTIC PLANNING

For many, the kick off of a financial planning process is typically done in anticipation of a life-changing event such as the sale of your business. And a look forward should begin with where you are.

An assessment of your current situation should include such considerations as what you earn, how you spend and where your assets currently reside. This then qualifies your long-term needs by outlining your family's current and future lifestyle requirements. Analyzing this information and aligning it with a clear articulation of your investment risk tolerance gives you a clearer picture of what your financial independence looks like.

FINANCIAL ROADMAP

A financial roadmap is a strategic planning tool that helps you navigate your way to and through financial independence. There are different iterations of financial roadmaps but the good ones will include analysis of the following areas:

- **Business Pre-Sale Planning**

For entrepreneurs, selling a company represents significant challenges but also the potential for great reward. Business founders must take the proper steps to maximize the company's valuation, maneuver high-stakes negotiations and protect themselves and their families from any liabilities once the liquidity event is complete. Tax implications (described in further detail in the next section) must be considered and gifting strategies must be thoughtfully outlined. Before selling, founders must first consider their cash flow needs which are almost always higher than initially expected. It's also important to put the family estate in order. This means a family mission statement should be drafted, all assets must be properly tilted and transferred into proper trusts and an outline of how much money children are to receive, at what ages and under what circumstances should also be created.

- **Tax Planning**

Tax implications surrounding the sale of a business are of course a significant concern and should be addressed well in advance of any final sale. Timing is critical. Depending on how your company is structured when it is sold - LLC, C-Corp., S-Corp.–and what state the business owner resides, you could experience different tax implications. Early in the process, the business owner should meet with a tax expert to ensure the corporate structure is set up to be most tax advantageous and determine if a change of residency is warranted. A good plan will also account for personal income taxes. With individual rates over 40%, taxes take a big bite out of your financial returns. Tax planning is best done with a long range view in mind. Not only is it about what taxes you pay today, but also how taxes might affect your plan in the future and after significant life events, such as a job change, retirement, a move to a more tax-friendly state, etc.

THE MAGIC NUMBER

Careful planning will effectively position your business for sale however you shouldn't stop there. Knowing where you are today and where you want to go requires a comprehensive understanding of what you have, what you will earn, what you want to be able to spend, and your risk tolerance parameters. This information allows financial advisors to then create a detailed plan that pinpoints when, and if, your current strategy will get you to your the amount of wealth you need to be financially independent – otherwise known as your 'magic number.' It will tell you if you've created enough wealth to spend the amount of money each year required for the lifestyle you seek without working.

In some cases, that number hasn't been reached and your advisor can make recommendations on how to reach that magic number. In scenarios where your magic number has been reached, recommendations within your roadmap are more focused on sustaining your financial independence over time. Other areas to consider include:

- **Legacy Planning**

Another important component to your financial road map is legacy planning which is less about deciding who receives what and more to do with how families live with their new found wealth. It isn't just preparing the assets for the family, it's actually preparing the family for the assets. Guiding the next generation to live the legacy the wealth creator intended is important work that first includes agreement and clear articulation of the family's core values. A mission statement is often created through a series of family meetings that creates the basis for all decisions.

Improving family members' financial literacy is an important component, as well as how to make decisions on family philanthropy. Many people have a hard time talking about wealth with their children. Advisors can help align wealth holders and spouses on important financial topics and advise on how to talk about those subjects with their children. The goal is to point individual family members toward a successful, fulfilled life. Your financial plan can and should be a life plan too.

- **Investment Planning**

Investment planning should consider risk tolerance and reasonable estimates of probable returns. Many plans will be based on linear returns rather than fluctuating markets. For example, if a plan assumes a 5% return on equity investments, a good plan would not take the linear approach and just assume your equity investments will earn 5% each and every year. That result is extremely unlikely. Although you may earn a 5% return over ten years, it is unlikely you will experience an exact 5% return in any year. Your returns could be 5%, then 3% then 10%, then -2%, etc. Anticipating that markets are volatile and cannot always be predicted is essential to a good plan. Using simulation software such as Monte Carlo, allows your plan to succeed no matter what the markets bring in any specific year.

At the conclusion of the investment planning process, an Investment Policy Statement should be prepared. This joint-signature document becomes a governing document that can be used to hold both investors and advisors accountable to the strategies within the investment plan.

- **Estate Planning**

Most common to the notion of estate planning is how best to save on estate taxes. While allowing the government only what they are entitled to should, of course, be a key consideration in good estate planning, the process should encompass more than estate tax considerations. Estate planning should also focus on safety of assets and ensuring your wealth transfers in a way that recognizes your unique goals and objectives. How inherited wealth will affect your heirs is a concern of most individuals. Sudden access to great amounts of wealth can often have a negative effect on the recipient, unintentionally deterring them from hard work and life experiences. Knowing and planning for these pitfalls is essential in assuring wealth lasts over multiple generations.

Thoughtful consideration of how to best provide for the wealth creators' children, grandchildren, elderly parents, siblings and more extended family members is a significant factor in estate planning. Preventing predators and creditors from unfairly taking advantage of estate beneficiaries is too.

SUSTAINING FINANCIAL INDEPENDENCE

A financial roadmap is both directional and collaborative for the benefit of all family members. It's also an important accountability resource.

Financial plans also evolve. Lives are dynamic and ever-changing, of course, and modifications will need to be made over time. Advisors at PagnatoKarp schedule quarterly meetings with their investor clients for this purpose, as well as an annual review. Face-to-face meetings with your advisor are essential to be certain all parties are on the same page.

Regardless of what your financial independence looks like, a key take away in the planning process is to set the bar very high. Don't guess on how much you need but be certain with a comforting magic number and smart financial plan. Exercise caution; use sound judgement. Discipline is required no matter how much money you have.