

Our mission is to shepherd as many business owners as possible to fulfillment of their goals and their ideal lifestyle.

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Do You Have a Value Gap and How to Close It

by

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What is a Value Gap?

A value gap is a term commonly used by business exit planners that describes the difference between the current value of a business and the value it needs to be for the owner to be able to achieve his or her post-exit goals. It is actually a bit more complicated than that because the exit planner is more focused on what the owner will net from ownership transition than the transaction value. So, taxes, fees, funding, and other considerations are a part of the value gap assessment. The value gap also is directly related to the exit strategy the owner decides to execute. There are about 34 of those.

How to Know if You Have a Value Gap

Whether or not you have a value gap, and, the extent of the gap can be determined by gathering some important information. Here are some basic steps to take:

- Determine what your lifestyle will be like after you leave your business.
- Put together a list of your post-exit annual expenses based on the lifestyle you envision. Give this some serious thought because you will probably have expenses that you do not have now, such as extended travel, more hobbies, and maybe maintenance of a second home. Some of your current expenses might be curtailed or eliminated such as annual funding for college and other expenses for your children such as car insurance and maintenance.
- Put together a list of capital expenditures such as down payment for a vacation home, gifts to children and grandchildren, and gifts to non-profits.
- Find out what your business is worth today. You might not need a full-blown business valuation at this point depending on the facts about your business and how you are likely to exit.

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- Have your exit planner prepare some calculations to determine what net proceeds you can expect from your ownership transition, the amount of cash you will receive up-front, and what you will receive annually and over what period of time.
- Have your exit planner give the above figures to your financial advisor, preferably in an Excel spreadsheet. The advisor will enter those figures in your lifetime cash flow projection which includes taxes and inflation. This calculation will include income from your other sources of income such as a 401(k), and your investment portfolio which you currently have, or will have when you exit. Be sure your advisor prepares a calculation that takes into consideration the death of you and your spouse to be determine if the surviving spouse's lifestyle will be sustainable. This is especially important if any income will cease at the death of the first to die. Have your financial advisor prepare a calculation to demonstrate the effect on your cash flow if one or both of you should require care, such as assisted living or in-home care.

What to do if You Have a Value Gap

- Look for ways to reduce taxes due when you transition ownership
- Consider other exit strategies that will net you more cash to be invested
- Consider a different investment strategy for the net proceeds
- Work with a consultant to increase the value of your business

How to Increase the Value of Your Business

Since your business is likely to comprise at least 90% of your total net worth, as it does for most business owners, invest prudently in your business to increase its value. There are about 55 value factors to be considered. Have your exit planner do an analysis of your business to determine what can be done. He or she can also help you determine the value factors to be addressed and in what order based on the associated costs, anticipated benefits, and how long before you wish to be out of the business.

When to Address the Value Gap

Today would be a good time to start. A prudent business owner will run his business every day as though he will exit tomorrow. All exits are not voluntary. By taking charge now, even an involuntary exit can have a positive outcome.

Joan M. Ridley is president of Business Wealth Solutions, a Dallas based advisory firm that consults with business owners about how to successfully grow and harvest their business wealth. Please visit our website at www.businesswealthsolutions.net. Calls us today at 214.692.9192 for a complimentary meeting to learn how we can help you. Ask for our complimentary brochure.