ACTIVE PRACTICE UPDATES

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Leaving your business

Every business owner should have a personal exit plan. We sometimes refer to this as a 'starting with the end in mind' strategy.

Whatever thoughts you have concerning the sale of your business, creating and putting into practice appropriate strategies is essential if you want to secure the maximum reward for taking the risk of being in business.

Key issues to consider could include:

- passing on your business to your children or other family members, or a family trust
- selling your share in the business to your co-owners or partners
- selling your business to some or all of the workforce
- selling the business to a third party
- public flotation or sale to a public company
- minimising your tax liability
- what you will do when you no longer own the business
- whether the new owners will need or want your involvement after the sale
- winding up.

Selling your business

If you consider your business to have a market value, or if you want your business to provide you with a lump sum on sale, it is essential to start planning how you will realise that value. This is particularly important if you envisage selling your business within the next 10 years.

Personal factors

There are many personal factors that are likely to influence when you sell your business. These may include:

- have your life goals changed?
- when do you want to retire?
- if you are selling within the family, when will you sell and how will this transfer/sale be funded?
- has your health begun to deteriorate?
- do you still relish the challenges of running your business?
- does your business have an heir apparent?
- will your income stream and wealth be adequate, post sale?

Business factors

External factors can also be important in timing your sale. If you can time your business sale to coincide with a period of economic growth, when buyers outnumber sellers and will pay premium prices, you will most likely secure the best price.

The current economic climate is much more buoyant than it has been for a number of years. As a result, there are a considerable number of companies looking to buy as well as hedge funds looking to build a portfolio of business groups. The following questions may assist in assessing the climate for selling your business:

- what is the impact of the current state of the stock market?
- to what extent is your business 'trendy' or at the leading edge?
- do your business forecasts show increases to the top and bottom lines?

Preston Park House South Road
Brighton BN1 6SB
01273 701 200 info@plusaccounting.co.uk

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- is your business doing better than other similar businesses?
- is your business at, or near, its full potential?
- are there prospective buyers?

You should assess the strengths of and opportunities for your business.

Selling your business is a major personal decision and it is essential to plan how you will maximise the net proceeds from its sale. When might you sell? Who are the prospective purchasers? What are the opportunities you have to reduce the tax due on the sale?

Maximising the value of your business

Whoever buys your business will want to be clear about the underlying profitability trends - is your profitability on the increase or decrease? You should be able to provide up-to-date management accounts and forecasts for the next 12 months to prospective purchasers.

The value attributed to many businesses is driven by the historical profits and therefore a rising trend in profitability should result in an increase in the business's value.

Maximising profitability

Increasing profitability is always important but no more so than in the years leading up to the sale. So, what is the range of values for your business? Although you may think you can make an educated guess, a professional valuation gives you more solid ground. These are the sorts of questions a potential purchaser might ask:

- are sales flat, growing only at the rate of inflation, or exceeding it?
- to what extent does your business depend on the health of other industries or of the economy?
- what is the outlook for your line of business as a whole?
- will your company's products and processes be outdated in the near future?
- how competitive is the market for your company's goods or services?
- does your company have to contend with extensive regulation?
- are your company's products and services diversified?
- what are your competitors doing that you should be doing, or could do better?
- will key staff remain after the sale?
- how does your company 'fit' with the purchasers?

These factors will all have an impact on the price-earnings ratio – the price per market share divided by the annual earnings per share. This, in turn, will determine the market value of your business.

You need to weigh up the factors which might influence the right time for you to sell your business.

Entrepreneurs' relief

When you raise that final sales invoice and bank the proceeds from the sale of your business, you should be completing one of the last steps in a strategy aimed at maximising the net return by minimising the capital gains tax (CGT) on sale.

Entrepreneurs' relief applies to sales of a whole or part of a business. This relief does not apply to the disposal of assets. There are specific circumstances under which the relief can apply to such a disposal, but these are related to the disposal of the business in which the asset is used.

Entrepreneurs' relief has a lifetime limit of £10 million for a reduced rate of CGT. The effective tax rate is 10%, giving a maximum tax saving of £1,800,000. As this is a lifetime limit, each disposal uses up relief which would otherwise be available for subsequent sales. The types of disposal which attract relief are:

- the sale by a sole trader of his or her business as a going concern (including incorporation)
- the sale of chargeable assets which were used by a sole trader in his or her business, which has ceased trading within the last three years
- the disposal by a partner in a partnership of his share in the firm, or of part of his or her share
- the disposal of shares and securities in a company, to which further conditions apply.

Where the business disposed of is run through a company, the seller must own at least 5% of the ordinary share capital of the company which must entitle him or her to 5% of the votes; he or she must be an officer or employee of the company, and the company must be carrying on trading activities, and to no substantial extent any other activities.

There is also relief available on the proceeds of winding up or dissolving a former trading company, provided this is done within three years of ceasing trading activities.

Contact us to discuss a strategy for exiting and selling your business.