Creating an Exit Strategy for Your Business

If you own a business, the thought of closing it down or selling your interest is often the last thing on your mind. But unless you plan on cheating death, a well structured exit strategy is a must. Exit strategies, which are usually embodied in the written agreements among the business owners, are not a substitute for a properly drafted and signed Will. Exit strategies embodied in an agreement will not effectively dispose of an owner's business interest upon that owner's death.

Instead, an exit strategy establishes the rules and guidelines for dealing with an owner's interest if that interest is transferred – whether voluntarily or involuntarily (*e.g.,* because of death, divorce, bankruptcy, *etc.*). Because many closely-held businesses serve as the primary source of wealth and income for the owners' households, exit strategies are among the important additional estate planning tools for many business owners.

Many partners may agree in principle that both should be taken care of in the event one decides to leave the business. But without an established agreement for how the departure will be handled, the parties may encounter difficulties in fairly compensating the departing owner. Or worse, they may end up being unable to agree, leaving all parties in an uncomfortable forced partnership. However, if properly structured, an exit strategy can help establish guidelines for dealing with an owner's interest and help prevent as much disagreement as possible.

So what exactly does a well planned exit strategy entail? It depends. Every business is as unique as the owners who manage it. Thus, every exit strategy should be specifically structured to meet the needs of the individuals involved. Even the most basic business can benefit from a well-planned exit strategy. For example, a lemonade stand with two partners may not need to purchase insurance to fund a departing partner's buy-out, a strategy appropriate to a more complex business. But it will still require a plan for compensating the departing partner when that partner can no longer carry on the business, or when an heir, spouse or bankruptcy trustee becomes the owner of the interest held by the departing partner. While each strategy will vary from business to business, well-developed plans will generally address restrictions on transferring ownership, develop a method of paying for the departing owner's interest, and resolve deadlocks in valuing an owner's interest.

The cost of creating a well-drafted exit strategy is relatively low in light of the benefits it provides. Negotiations regarding valuing a partner's interest, compensation for intangible assets, and plans for the business's future can cost thousands in legal fees. By defining a strategy in advance, all parties can create a plan that meets their goals in a more objective and fair manner.

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If your business lacks a well-planned exit strategy, it's time to begin the process. Owners need to address both business and personal goals to properly structure a plan. Because there are both legal and tax implications involved with exit strategies, owners should consult both their attorneys and their tax advisors before finalizing an agreement. Many owners may find that they have different ideas when it comes to the future of the business. But with the help of good advisors, owners can create a plan that treats all parties fairly when an owner leaves.