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Determining How Much Wealth is Needed After the Business Exit

Michael Wildeveld, CEPA, M&AMI, CM&AP, CM&AA, CBI, CBB
michaelw@veldma.com

Veld Mergers & Acquisitions
www.veldma.com
1 Park Plaza, 600
Irvine, CA 92614
310-652-8066

When creating an effective, tax-efficient wealth transfer strategy, you should focus on three basic issues that should be resolved for successful wealth preservation planning to occur. These issues include:

1. Fixing your financial objectives before considering a wealth transfer.
2. Determining the amount of wealth to be transferred and identifying how much is too much.
3. Designing a wealth transfer strategy that keeps the IRS from becoming the largest beneficiary of your hard-earned cash.

One of the primary decisions every business owner makes when transferring wealth to children is not how to accomplish the transfer, (that's the estate planner's job) but *how much* wealth to transfer to the children. Answering that question requires that you first revisit your own exit objective; namely, how much wealth you wish to have after you exit your business. The amount of wealth owners wish to leave to their children usually (but not always) depends on how much the owners wish to keep after they exit their business. As a general rule, we discourage parents from making significant gifts to children until their own financial well-being is assured. Only after the parents' needs are met do we ask how much is enough—or too much—for the kids.

The first step in the Seven Step Exit Planning Process™ is for owners to determine their objectives. Owners who fail to do so are rarely able to leave their businesses in style. The three exit objectives that every owner must fix before they are able to progress further in transferring wealth to their children are best phrased as questions:

1. How much longer do I want to work in the business?
2. What is the annual after-tax income I want (in today's dollars) during retirement?
3. Who do I want to transfer the business to?

As you can see, answering the second question establishes personal financial goals, and it also provides the takeoff point for how much money you can afford to leave to your children. In order to create a realistic income objective, you and your advisors may have to make some assumptions along the way. The

assumptions that you and your advisors may need to consider include:

- Anticipated rate of return on investments
- Inflation rate for future years
- Projections regarding the strength of the local economy to support your business prosperity

When advisors typically discuss with owners the amount of money they think it will take to meet their financial security goals, they usually find that owners have picked a number out of the air: *"I need $2 million in cash for my business."* This number usually bears little relationship to the owner's true needs. It is important for you to draw upon the expertise of an Exit Planning professional to work through your financial objectives and the assumptions associated with achieving them so that you can get a realistic picture that aligns with your financial needs. By using "what if" scenarios with different variables, your advisor can help you determine how much money you will need from the sale of your business.

After you have determined how much wealth you wish to have after you exit your business, you are more prepared to proceed to the next step for designing a family wealth transfer strategy that helps meet your overall exit objectives.

If you have any questions about transferring wealth to children, please contact us to discuss your particular situation.

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