

The 5 D's

Did you know that 79% of business owners have no written transition plan and 48% have done no exit planning at all?* And on top of that, roughly 50% of all business exits are involuntary and are forced by dramatic external factors.* It is important to have a well-thought-out plan of what happens if something unexpected happens to you or someone in your family, directly impacting your business.

Owners need to plan for how they want to walk away from their business not only in a perfect scenario, but also in a worst-case situation. Throughout the exit planning process, it is critical to consider the following scenarios that force owners to exit their business hurriedly, and often leaving value on the table. They are often referred to as the 5 D's:

- Death
- Disability
- Divorce
- Disagreement
- Distress

We often think that a will addresses the needs upon the death of an owner. If your partner or spouse passes, do you have the ability to continue their job at the level they were performing it? If you're put in a position where you need to stay home to take care of a suddenly sick or disabled family member, what will happen if you are forced to exit your business due to your inability to come into work?

It is important to address the tough questions about what you want to happen to your business if you have to exit your business prematurely. Statistics have shown that in the four years following an owner's death, sales declined 60% on average and employment fell 17%, resulting in a decrease of the overall valuation of the business.** Additionally, two years after an owner's death, firms are 20% more likely to fail or file for bankruptcy.**

It is important to have a plan in place to help reduce the risk of these issues happening to your business in your sudden absence.

What do you want your family, clients and management team to know? What do you want to happen if you were to die or become disabled? What should happen if you or your spouse wants a divorce? What happens if there is a disagreement between business partners? An unplanned exit can not only impact the day-to-day operations of your business, but can also affect the tax and legal aspects of it, along with the value of your company. You need to create contingency plans for each of the 5 D's to be properly prepared for any unplanned scenario.

While each of these unplanned events will undoubtedly be treated differently, an important step to take is creating and communicating the action plan for each contingency. This can be achieved through a contingency letter, which serves as a playbook that is a shorthand to your operating agreement and your estate planning documents. Your contingency letter should outline what you, as the owner, would like to happen if you can no longer operate the business.

Have you planned for these contingencies? Some of the largest risks to the business can be planned for and some cannot. These are events that are usually out of your control and can inhibit the value of your business.

*Exit Planning Institute State of Owner Readiness Report 2013

**Becker, Sascha O., and Hans K. Hvide. Do Entrepreneurs Matter? 2013

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