

Using A Tax Minimization Analysis: How to Best Advocate For Clients Selling Their Business (Part 1 of 2)

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If your business was to sell today, how much cash would you walk away with? Moreover, what is the tax impact you would incur and what is the best structure and purchase price allocation to avoid such tax impact? Essentially, how do you reap the maximum return on selling a business you've spent your life building? A Tax Minimization Analysis (TMA) is the answer. A TMA analyzes a multitude of factors that play a vital role in the outcome of selling a business. When executed properly, a TMA will allow a seller to understand the financial breakdown on every level of a merger, acquisition or business succession. Additionally, the TMA will provide an accurate calculation taking into account all transaction factors and variables that affect the cash a seller obtains at closing and post-closing. At The Center for Financial, Legal & Tax Planning, Inc., (The Center) we have found the TMA to revolutionize M&A transactions as it provides the transparency a seller deserves and the information necessary for our team to best advocate for your desired outcome.

As many know, an M&A transaction can be overwhelming with the multitude of variables that drastically influence the outcome. The variables include, but are certainly not limited to the overall structure of the transaction, the asset/stock basis of the selling company, ownership configurations, real estate involvement, multiple entity involvement, liabilities paid at closing, purchase price adjustments, earn-outs, consulting fees, recaptured depreciation, and the federal, state and local tax impact. Each variable listed can severely impact the outcome of a transaction and each must be taken into account as early in the transaction as possible. When all variables are understood early in the transaction, your counsel is best equipped with the knowledge to understand how to best combat or strategically use such variables to obtain an outcome that not only protects a seller legally, but minimizes their tax burden to the fullest extent possible. After all, we did not invest our lives into a business to give thirty to fifty percent of the closing proceeds to Uncle Sam when it's sold! The example below provides some insight into the value of a TMA.

A TMA can not only pay for itself through the tax savings it will discover, but potentially pay for the merger and acquisition (M&A) team you engage for your transaction. For example, you're selling a business in an industry that deals with complex licensing or regulation (transportation, sand & gravel, chemicals, etc.) and the Buyer seeks an asset sale for the benefits of immediate depreciation. Through proper execution of a TMA, your counsel can analyze and determine the best structure of the transaction, whether it be an asset, stock or in this case a potential 338(h)(10) sale. The TMA will calculate the tax effect of each sale type (asset, stock, and 338(h)(10)) to determine what structure best suits the seller from a tax standpoint. Under this example, the TMA may determine the 338(h)10 will best overcome the complexities of assigning licenses or permits while also providing the paramount tax outcome for not only the seller, but in this example the buyer too.

However, the example continues and the buyer now seeks to allocate more than book value to the seller's equipment rendering the seller subject to recaptured depreciation (taxed at the rate of ordinary income). Here, the TMA would not only provide the threshold amount subject to recaptured depreciation but it would allow the seller to determine alternative negotiation strategies to help avoid the negative tax impact caused by recaptured depreciation. Then, when the purchase price allocation is agreed upon and in place, the TMA will analyze factors outside the transaction that impact its outcome. Factors such as other income within the tax year of the transaction or loss carryforwards, both of which can play a vital role in the overall tax impact. This example, while simple, displays the value in the TMA illustrated in its transparency and ability to balance each factor and variable that play a role in the outcome of a transaction. There's tremendous value and comfort in providing sellers an evolving transparency of their transaction.

At The Center, in our forty plus years of M&A experience, we have come to realize the value in analyzing every factor that plays a role in the outcome of a transaction. More specifically, this value is derived from the TMA's ability to evolve such factors as the transaction progresses in order to give full insight and transparency to the seller. This insight not only provides a sense of comfort to sellers but also offers a strategic advantage in achieving the desired result. A TMA will allow an open dialogue between counsel and client in regard to goals and strategy while ultimately delivering the most advantageous structure possible when selling your business. If you are thinking about selling your business or in process of selling your business, allow The Center to analyze your transaction using a TMA so we can confirm you're obtaining the greatest outlook possible in your sale.