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 by Michael Gentry

Shifting Focus: Preparing for a Monetizing Event

Creating wealth vs. wealth preservation.

Great entrepreneurs generally possess certain qualities, including perseverance, concentration, drive, focus, and grit. These attributes often serve as the foundation for their success. Given that entrepreneurs are generally above-average risk takers, they are typically willing to invest nearly every resource they have into the success of their business: time, money, energy, and "sweat equity," to name a few.

Inevitably, however, most entrepreneurs at some point in their careers will pause and take stock. They may find themselves thinking through the development of a succession plan, the achievement of personal and professional goals, or potential exit strategies. Upon reaching a certain level of success, the preservation of wealth may become a more essential focus than wealth creation. The decision-making process is unique to each individual, but a few general themes permeate discussions with entrepreneurs at this stage.

Planning Considerations. No matter what strategies or time frame one considers for a monetization event, the single most important factor is effective planning. This cannot be stressed enough. Professional advice can help business owners prepare by gathering the necessary information to evaluate strategic options, whether through an outright or partial sale, recapitalization, initial public offering, Employee Stock Ownership Program ESOP or some other form of succession planning.

Risk-taking can build a business. But it's not a good strategy for managing the wealth you've created.

Long-term thinking should dominate discussions around strategic alternatives and ultimately, the management of wealth created by an entrepreneur. As entrepreneurs navigate this process, it is important they ask themselves some difficult questions and have in-depth discussions with advisers regarding long-term personal, professional and financial goals. These topics should include both qualitative and/or emotional factors in addition to quantitative and financially driven dynamics, which can sometimes be highly conflicting forces. This process is both art and science, and self-reflection and introspection can go a long way in determining a prudent course of action.

A Coordinated Approach. A pragmatic, disciplined and thoughtful approach is necessary for the evaluation of strategic options and thinking through the build-out of a comprehensive financial plan. Effective communication and coordination between a wealth adviser, estate planning attorney, accountant and other members of an advisory team are vital to a successful outcome. Far too often, this coordination is lacking and each of these teams remains siloed, with little or no communication. Getting these parties in the same room can be the single best way to efficiently and effectively evaluate alternatives. Coordination among the advisory team is critical to understanding how their advice and decisions impact available options and ultimately, a long-term plan for an entrepreneur.

Diversification and Risk Management. Investment portfolio diversification is a cornerstone of financial management, but can prove counterintuitive to entrepreneurs. After all, many entrepreneurs have created their wealth through the very antithesis of diversification: a concentrated position in their businesses.

An argument can certainly be made that an owner's capital is best served invested in the business to fuel growth and set a solid foundation for sustainability. However, as business owners' priorities transition from wealth creation to wealth preservation, it is prudent to consider their investment in the business and the need to diversify holdings to manage their overall risk and enhance the probability of wealth maintenance over time. Entrepreneurs become wealthy by taking risk; they stay that way by diversifying.

Entrepreneurs often underestimate risk exposures while overestimating diversification. A thorough comprehension of risks starts with understanding the market cycle of one's largest asset, the business, and how it may behave in comparison to other types of financial assets. For example, if a business is highly cyclical and correlated to the health of the economy, one may want to consider complementary investments in other asset classes, such as equity exposure in more defensively positioned and non-cyclical sectors, investments in fixed income or an allocation to alternative strategies.

Whether considering outright sale or simply taking some "chips off the table," risk management needs to be evaluated through a much different lens than risk management in one's business. Factors such as liquidity planning, insurance coverage, lending strategies and cash-flow management should also be evaluated in the context of risk management. Implemented effectively, consolidation of these factors may lead to less volatility, lower overall risk and a higher probability of success.

Financial planning and long-term wealth management is difficult and complex. For entrepreneurs, who understandably have been laser-focused on the growth and success of their businesses, managing through a liquidity event can involve a major shift in mindset and focus. Thorough planning can ensure that the hard work, time and dedication put into building a business is protected and managed in a way that allows one to sleep well at night and focus on the next set of goals, whatever they may be. I

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