

Dealer Transfer Series: Planning Before the Transfer

The moment has arrived. After many years of hard work and countless conversations with family and other owners, you made the decision ... I'm going to sell my dealership. But now what? Making the decision to sell your dealership is often the hardest part of the transfer process. But once that decision is made, other issues must be addressed to help you create a strategy before negotiations begin.

Valuation. What is your dealership worth? Does the value match up with your expectations? Many factors determine value, including asset values, profitability and ease of financing. Sellers should consider hiring a valuation expert to take these and other factors into account and gain insights on industry valuation trends. SWA Financial Consulting is the firm I recommend due to its industry knowledge and experience in conducting equipment dealer valuations. For more information on SWA Financial Consulting, you can contact Curt Kleoppel at 816-561-5323 or curt@swassn.com. **Context.** After assessing value, consider the context of your situation as it may impact the timing and structure of a transfer or the price a buyer will pay. Questions to help you assess context include:

- Do you have market share issues? Is termination of your main line dealer agreement likely?
- How many potential buyers exist?
- Has your manufacturer told you who may be permitted buyers? ("permitted" buyers should be your preferred buyers unless a large value gap exists)
- What is your appetite for remaining in business? (impacts use of merger as a potential transfer structure)
- Is one of your locations a "closed point"? (fair dealership laws play a role, but this factor may reduce valuation, including a reduction in dealership real estate value)

Taxes. Consult your attorney or other tax advisor to understand the impact of taxes on your deal. Structure decisions can impact dollars in your pocket after taxes are paid. Some common issues impacting taxes include:

- *Asset vs. Stock Sale.* A stock sale represents the best tax consequence for a seller because the proceeds are taxed at lower capital gains tax rates. Sellers normally pay higher rates of taxes if the dealership sells its assets. Unfortunately for sellers, buyers may refuse to buy stock because it requires a buyer to assume your liabilities, can limit the ability to use manufacturer floor planning to pay for part of the purchase price and the ability to reset asset values for purposes of depreciation is generally not available.
- *Type of Entity Matters.* Is your dealership an S corporation, partnership or limited liability company? If so, the tax difference between an asset sale and stock sale is minimized. The reason for this is that much of the taxable purchase price paid in dealership transactions are tied to the real estate or "blue sky" and result in taxes at capital gains tax rates to the individual owners of the dealership.
- *What about C Corporations?* Many dealerships remain in C corporations. C corporations pay a separate income tax from the owners of the business and create a "double tax" in an asset sale. Unlike other types of entities, purchase price payments to a C corporation are subject to one tax rate that is significantly higher than the capital gains tax rate. To top it off, Uncle Sam will also

charge the owners a second tax when the dealership distributes the money to the owners. Through planning, it is possible to minimize some negative tax consequences, but the unfortunate truth is that C corporation dealers often keep less in their pockets. *Planning Note: if a sale is a few years away, contact your attorney or tax advisor about potential benefits of converting a C corporation to an S corporation.*

Merger?

- *Benefits.* Mergers between dealerships can usually be accomplished on a tax-free basis. It is also possible to buy out certain owners in a merger (the selling owners would pay tax). In most cases, mergers don't require payments or additional debt, meaning that the equity levels of the dealerships won't be impacted. This helps dealers maintain minimum equity levels required by some manufacturers.
- *Complications.* Mergers are more complicated because the parties will continue in business together. This means that each dealer must carefully review the operations of the other dealer(s) to understand what they will have after the deal closes. Negotiation of a buy-sell agreement between the owners is also critical (to be discussed in my next two articles) and you should never underestimate the challenges of integrating multiple companies and creating a shared culture after closing.

A decision to sell is only the beginning. By understanding your options and doing some advance planning, you will be able to develop a "sale" strategy that is best for you.