Closing a business

Question: How do I close a business?

Making the decision

While every aspiring business owner starts a new enterprise with dreams of success and growth, it's wise to know how your small business ownership story may end before you begin. When and how you plan to exit can make a big difference in how you manage your new company throughout its life.

Closing a business need not be a negative experience. It can mean new opportunities, a long-awaited retirement or the chance to gear down as an employee for someone else, leaving the management and ownership challenges to your employer.

Or, a business closure can be the result of less pleasant situations involving the health of the owner, an economic downturn or increased competition. Whatever the reason, being prepared for a closure with a sound exit strategy ensures you can enjoy business ownership knowing that if an exit becomes necessary, you'll be ready. When the time comes, you'll have several options.

How do you know it's time?

There are several warning signs that may indicate to you it's time to change or close your business.

One is if your debt-to-asset ratio is on the rise. Every business occasionally has to borrow money to purchase equipment or other assets. However, if your debt as a percentage of your assets is consistently on the increase, you could become over-leveraged. Some experts say the magic number is 50 percent.

Likewise, a rising level of debt-to-shareholder-equity indicates that a company's leverage is increasing. While a wise use of leverage is a part of standard business practice, the greater your leverage, the more unstable your business and the less equity you maintain in the company.

Another red flag is when you are losing money in ever-increasing amounts. Showing a tax loss is not necessarily a devastating blow, but if your company is losing money in "real
terms," you may have a problem. It's not uncommon for businesses to lose some money in their early years, but if those losses increase rather than decrease in time, you may not be able to overcome them.

Another sign is when your inventory turns over more slowly as time passes. If items remain on your shelves too long, you may be heading for trouble.

And, if you're having trouble raising money for your business, it may be a sign that things are going as well as you'd like to think. Your banker may be attempting to help you see the writing on the wall and stay out of deeper trouble.

The final sign—and some might say the most important one—that you may need to consider transitioning the business is when you stop having fun running it. You must enjoy what you're doing, or you will resent the enormous sacrifices that business ownership demands. If you're finding it hard to go "to the shop" every day, then you might want to reflect on your future with the business. Life is too short to spend it doing something you don't enjoy.

So, what are your choices?

One is to pass the business to children or other family members. Or, you may want to sell the company. You could choose to liquidate it and sell the business assets. Or, in the worst-case scenario, you could end up filing for bankruptcy to deal with substantial debt.

As you plan your strategy, consider how what you plan to do tomorrow affects your business today. For instance, you may want to hand the company off to a family member, but is that person qualified? Does she need training? Does he have the interests and innate abilities to be successful? Will you truly be able to hand the reins over to someone in the family without feeling as if you need to maintain some control?

If your plan is to sell the company, you will want to take steps to constantly enhance the value of the company in terms of facilities, assets and networks. Selling to a partner or even a competitor who already has systems in place might mean you want to put your investment in product lines and increasing the customer base.

Preparing from the beginning

Like most things in life, timing is everything. Remember that you opened the door to your

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business so you could have the independence, autonomy and pure enjoyment that come from being your own boss. The day that business ownership ceases to be a pleasurable experience (even with its innate challenges) is the day you should begin your exit strategy.

Starting your business wasn't an easy process. But as challenging as that was, exiting may be even more so. It will depend on whether or not there is a market for the company and whether or not the price that the owner believes to be fair is considered fair in the marketplace.

This, of course, puts a great deal of emphasis on the valuation of the business prior to a sale. Since there are many approaches to valuing a business, it should be done in a way that is fair to both buyer and seller.

From your first day of business, bookkeeping should be clear, consistent and comprehensive. Your records should be something you'd be proud to show to a prospective buyer. With a good set of books in hands, valuation is much easier. Be wary of undervaluing the business—a common mistake.

An important element of your exit strategy should be your personal plans. Give serious thought to the first day you awake and don't have to report to the shop for work. How will you feel? What will you do?

Chances are the separation will be a gradual one that involves training and transitioning of intellectual capital. In some cases, if you particularly excel at one facet of the business and would enjoy continuing to perform that function, the new owner might welcome your experience in that role. To avoid confusion and bad feelings, negotiate an arrangement that clearly delineates where your duties end and the new owner's begin.

If you intend to keep the business until you literally expire while working the counter, make it simple for your heirs and employees to continue through a transition. Insure the company and its assets sufficiently to function while the valuation and final disposition of the company are settled.

Although planning an exit strategy is important and should be as specific as possible, remember to stay flexible. Shifts in the market or in the community, changes in your personal goals, family situation or health or even the appearance of a better opportunity could change your strategy and timing.

Much like keeping your home presentable when it's on the market, managing your business everyday as if you are preparing to sell it will guarantee you are ready to seize the right opportunity at the right time.
The nuts and bolts

If you decide to sell or close your business—just as when you opened its doors—there is paperwork and there are certain procedures you must follow. The process can take anywhere from one week to several months or years, depending on the business size, its complexity and what you plan to do with it. If you have partners, the process may take longer.

Your first step is to vote to close the business. If you are a sole proprietor, this step is easy. There is only one vote, and it's yours. There are others with whom you might want to consult, such as a spouse or other family member, but in the end, you must make the decision alone.

If you have been doing business as a corporation, limited liability company (LLC) or partnership, you and your business associates must agree to dissolve the entity by following either the procedures set out in your organizational documents or the rules set out in the state's business statutes. Usually, these rules require at least a majority of the owners to agree on dissolution, but they could require a two-thirds majority or even unanimous vote. Make sure you record your decision with a resolution in the minutes of a meeting or with a written consent form.

If you have been doing business as a corporation or LLC, you will need to officially dissolve your entity so that you are no longer liable for business taxes or filings. Officially dissolving your business also puts creditors on notice that your entity can no longer incur business debts.

Forms

Necessary forms will indicate the disposition of your company's debts and liabilities, how the business assets will be distributed and how you and your co-shareholders elected to dissolve your business.

For Washington residents, the forms you need to complete your dissolution of a company can be found on the Washington Secretary of State's website at http://www.secstate.wa.gov/corps/ and the universal Washington State business access site http://access.wa.gov/business/index.aspx

For-profit corporations need to complete the following: Articles of Dissolution by Washington Small Business Development Center www.wsbdc.org

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Voluntary Action, Request for Termination and Resolution to Dissolve.

LLCs must complete Articles of Termination for a Limited Liability Corporation. Limited partnerships also require the Certificate of Cancellation of Limited Partnership, and Limited Liability Partnerships require the Notice of Withdrawal for a Limited Liability Partnership.

Of course, there are some federal forms you will need to complete as well. If you are a sole proprietor, this includes Schedule C: Profit or Loss from Business and Schedule SE: Self-Employment Tax. If you sell any of your assets, you will need to complete Form 4797: Sale of Business Property.

If you sell the business, you'll need to submit Form 8594: Asset Acquisition Statement Under Section 1060. Form 1099-MISC: Miscellaneous Income is required for each person to whom you paid at least $600 for services. If you're required to remit excise taxes to the IRS, you will need to submit Form 720: Terminal Operator Report with your final tax return.

For businesses with employees, two forms are required: Form 940: Employer's Annual Federal Unemployment Tax Return and Form 941: Employer's Quarterly Federal Tax Return. These are due in the quarter in which you pay your employee's for the last time. You should also provide W-2 forms to your employees for that calendar year. Finally, you are required to file Form W-3: Transmittal of Income and Tax Statements.

Most of the federal forms can be found on the IRS site at www.irs.gov/formspubs.

More forms and closing details

You will need to submit forms to the state of Washington regarding sales tax and pay the amount owned. Washington State business access site is http://access.wa.gov/business/index.aspx

You'll need to notify your local government office that your business is closing since you hold a local business license. Since each community or county is different, check to see if there are other forms to file or procedures to implement to complete your closure.

As one final protection from liability, you will want to put an announcement in your local media that you are closing or selling your business. This will ensure you are not held accountable for any future acts by a business with the same name.

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Pay all of your bills, and request letters from your suppliers indicating that you have paid in full. And if you have any outstanding receivables, you'll want to collect on those before you close the business. It's much harder to do after you close the doors. If you aren't successful in collecting those accounts, weigh the cost of legal action with the amount you are owed before pursuing.

Some start-up costs are tax-deductible in the year you close your business; check with an accountant.

In addition to accounting assistance, you may want to engage some legal assistance as well to ensure you have completed every step associated with dissolving your business.