Entrepreneurs in Transition: Key Considerations as You Plan to Leave Your Current Venture and Start Another

As our culture and collective work patterns evolve, job changes throughout a career are becoming more common. Today, an executive or entrepreneur can expect to work for or build multiple companies before ending a professional career. While this presents a myriad of opportunities for wealth creation, there are also challenges associated with each career transition.

Regardless of which stage of transition you find yourself in, take some time to evaluate key financial matters. The following considerations can help you maintain your financial security and focus on your new venture without compromising your short-term financial needs or long-term goals.

Before you leave your current company.

A well thought-out transition from your current company to your next company should include a few key components:

Consider paying down any floating-rate consumer debt.

If you are heading towards a period of reduced cash flow, consider reducing or eliminating credit card debt, home-equity loan balances, auto loans, or other types of debt that may be subject to rising rates. Eliminating these expenses may make your monthly outflows more manageable during your period of transition.

Build up your cash reserves.

If you are unsure of the timing of your next paychecks, creating a cash reserve can help you maintain your short-term liquidity needs during a transition. At a minimum, we recommend keeping six to nine months' worth of liquidity on the sidelines. This may be especially helpful if you are still in the process of evaluating your next opportunity.

Create or review your current monthly budget.

Revisit your monthly expenses prior to entering a period where you will be without regular cash flow. Are there any discretionary expenses that can be reduced or modified? This may also be an ideal opportunity to prioritize your recurring expenses.

Review your credit facilities.

Before you leave your current company and steady cash flow, make sure you have a credit facility that allows you to access capital in the event of a financial emergency. Often, these facilities are home-equity lines of credit and security-based lines of credit.

Recent tax law changes state that for home-equity interest to be deductible, the usage of the capital must be for home improvements. Whether you choose to use your home-equity line or not, it is important to set it up before you leave your current employment. Most banks will not offer new home-equity lines of credit if you are unemployed. However, you may consider a security-based loan as an alternative. Also known as a margin loan, this is a loan against your non-retirement investment accounts. The interest on the loan is deductible up to net-taxable investment income. For some, this structure is more attractive than a traditional home-equity line of credit.

While you are in a period of transition.

During the time between your previous and new employment, we recommend optimizing some of this time to review key financial planning issues.

Assess the options for your retirement plan.

You have everal choices for your next course of action for the retirement plan sponsored by your former employer:

1. Do nothing; leave your money in the current plan, if allowed. Many individuals take this course of action because it's the easiest, but it's not always the wisest.

2. Roll your assets over into a plan offered by your new employer.

3. Cash out your former plan and use the funds to help with current financial needs. This is the least-attractive option. If you are under 59 1/2, these monies may be subject to a 10% penalty, as well as ordinary income taxes.

4. Roll this money over to your own individual retirement account or IRA, also known as a rollover IRA. This course of action has desirable tax benefits, and offers a stretch out provision for non-spousal beneficiaries. This provision allows non-spousal heirs to defer distributing money and paying tax on it for the remainder of their normal lifetimes, enabling significant tax-deferred compounding.

Review and update your wealth transfer and estate plan.

This is an aspect of your financial plan that should be reviewed every three to five years if there is a meaningful change in your financial circumstances or wishes. As you review your wealth transfer strategies, consider the following:

1. Any recent, meaningful tax rule changes for gifts since your will was last updated. For example, there were significant changes in the new 2018 tax rules that raised the thresholds for gift and estate taxes.

2. A current or anticipated change in residency. States such as Pennsylvania, New Jersey and Delaware each have state-specific inheritance and gift tax rules. Your key documents should take these nuances into consideration and be updated accordingly.

3. Updating critical documentation, including:

    Will. This document determines and helps ensure that your assets are distributed according to your wishes.

    Power of Attorney, for yourself and your adult children. This document specifies the ability to sign on behalf of another if someone is incapacitated.

    Living Will. This document specifies the amount of healthcare coverage and efforts you desire to preserve your life.

    Guardians, if you have minor children. This specifies who would be responsible for caring for your children until they are of legal age.

Re-engage your network.

As you consider the direction and scope of your next opportunity, now may be an ideal time to reconnect with former colleagues and peers who may have insights and connections that could be valuable now and in the near future. To get started, we suggest refreshing your LinkedIn profile, posting content that is relevant to your industry, and proactively reaching out to centers of influence who may help you access new networks and professional connections.

When you're beginning your new opportunity

Before you begin your next venture, be sure to consider important financial matters as part of your evaluation criteria for new opportunities. These considerations can support your decision-making process, and help you identify the opportunity that aligns with your needs and long-term goals.

Assemble your advisory team.

You should surround yourself with professionals who have skill sets that complement yours. Your advisor team should include a senior mentor, certified public accountant (CPA), contract or tax attorney, CERTIFIED FINANCIAL PLANNER™ (CFP®) practitioner and insurance advisor. This team can serve as a sounding board for your current compensation package, and help you understand and compare equity compensation versus cash compensation, which can be useful in evaluating the outcomes of different models.

Understand your new equity stake.

If your new company is offering you, as a founder or senior executive, an equity stake, this presents an additional level of complexity. It is important that you understand the goal the company. Is it private or public? Is it targeting an acquisition, IPO, or growth and expansion? Is the equity an outright grant or is there a vesting schedule? If the company is already public, equity may be granted in the form of stock options or restricted stock units (RSUs). Options and RSUs are very different in terms of the ownership equity component they represent. You may also have access to an employee stock purchase plan that allows for favorable accumulation of shares over time. This information can help you develop the right strategy to monetize your equity in the future, as well as focus on specific tax nuances to help you derive an optimal outcome.

Review your new benefits plan and insurance options.

Before signing on the dotted line with your new company, it's important to carefully assess the life insurance, health insurance, disability insurance and retirement benefits relative to your prior company. Your next opportunity may not offer the same level of coverage or an equally robust benefits plan, especially if it's an earlier stage company with more of an equity ownership component. You may need to augment some of the insurance programs with personal policies to make sure your levels of coverage are where you need them to be. Supplemental policies can also be obtained from industry professional groups, as well as chambers of commerce.

Health insurance is usually a key component of evaluating new employment opportunities. It is important to review your potential new employer's healthcare benefits in terms of co-pays, prescription coverages and in-network physicians and facilities. It may also be worthwhile to compare COBRA costs and coverage with your new employer's health insurance plan.

You should also carefully consider the amounts and types of life insurance and disability income insurance that are appropriate for you. As your asset base increases and your liabilities decrease, your need for these coverages may decrease. Additionally, group polices offered through an employer can be costly and lack the specific type of coverage you feel is needed for your situation. If you are in an industry where changing employers multiple times in your career is inevitable, solidifying your own plans for life and disability income insurance may be more sensible that capitalizing on the group policies available through your employer. When you have your own personal life insurance and disability insurance programs, your premiums are fixed for the duration of the policies.

Additionally, personal policies give you the ability to specify the depth of coverage. For example, a personal, long-term disability policy gives you the ability to specify the roles and functions of your job that will determine the definition of disability. Under a group plan, the definition of disability becomes much broader and the benefit is taxable to you if you receive it. When you own your own policy and pay your own premiums, the disability income is received income tax-free.

Periods of transition can be challenging, exciting and a little bit scary. Taking time to thoroughly evaluate the numerous financial planning implications is key to helping you protect your family's financial well-being.

Whether you're considering a new opportunity or in the middle of a transition, the financial professionals at Sarian Strategic Partners are here to help you understand and assess your options so that you can make the right decision for your situation. Contact us today to learn more.

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