
Richard D. Mowrey's

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Creating Wealth Through the Power of Your Business

A Brief Guide To Selling Your Business with Minimum Stress and Maximum Profitability

Like any complex and critically important task, preparing your business for sale and ultimately selling your business will be much easier if you know what to expect and what to do to assure that you get it done right.

For a first time seller or even experience sellers, transferring the ownership of a business is a process that contains both unknown pitfalls and significant opportunities. Aside from achieving a fair price and favorable tax treatment, as a seller, you will want to know that you are putting your life's work into good hands.

This report was written to help answer some of the questions you may have about selling a business. It is designed to provide guidelines about how to go about selling your business, once the decision has been made. In the report, we will also suggest some questions you should ask to make the most informed decisions possible as you proceed.

Of course this can't be a complete guide. So if you would like further information, please feel free to give us a call our firm. We would like to help make cutting the ties to your business as **painless** and as **profitable** as possible. We know from personal experience that it's not just a job. It's your business. You've put years of work, worry, and money into it's growth, but at some point-no matter how tied to your business you are right now-you must eventually think:

"Is Now the Time to Sell."

Reasons? Maybe you're ready to retire. Maybe your company has grown bigger than you want to manage. Or maybe you're ready for a new challenge. When that time comes, you are likely to find yourself with a healthy supply of questions. Some of the typical questions most

business owners have are: "When should I sell my business?" "How do I locate a buyer?" "What should my asking price be?" "Who should handle the negotiations?" Here are some answers to these and other questions:

Q: When should I sell my business?

A: There are two equally important parts to answer this question. The first is from your own personal viewpoint:

When You are Ready to Sell

People sell their businesses for any number of reasons: To start a brand new venture, health problems, even burnout-they're just not interested in the business anymore. Some owners count on passing the business on to their children but find their children do not want it when the time comes.

Retirement fits into this list too, but if you are considering retirement, start planning well ahead. In fact, when selling for any reason, if possible, you should begin to structure the company for sale and start to identify potential types of buyers three to five years ahead of your target date for the sale.

The second part of the answer to the question of "When?" comes from a marketing and profit-making viewpoint:

When Your Business is Ready for Sale

It is easier to sell a business when it is doing well, improving regularly and in good financial shape. That is also when you'll get the best price and terms. Remember, **buyers invest in the future of a business but base their decision to buy on past performance.**

Many factors can influence the timing of a sale: Such as, the condition of the economy, current business trends (*what's "popular" in the market*), interest rates, availability of financing, etc. You also may want to adjust the sale plans to allow for the roll out of a new product that will have an impact over the next few years.

Q: Once I decide to sell, how do I find a buyer..or the best buyer?

A: As in any marketing problem, the first step is to analyze the situation and identify potential buyers. A key employee, a supplier, or a competitor might have an interest in acquiring the business. But...these three may not be your best buyer.

Consider All Your Own Contacts and Potential Networks

Most potential buyers fall into three categories: **individuals**, for the most part, buy businesses with a purchase price of under \$2 million and /or profits of less than \$500,000 annually. Businesses above this size generally require a down payment which is out of reach for most individuals.

Small corporations and **investment groups** make up the other categories. They seek out companies with a purchase price up to \$20 million. The **large corporate buyers** and **investment companies** usually look for a business with at least \$50 million in sales volume and/or \$5 million in per-tax profits annually.

Owners are often tempted to locate and contact buyers personally-though advertising, referrals, and their industry's "grapevine." Unfortunately, this is a difficult, time-consuming task and may not leave the seller in the best bargaining position. It can also compromise the confidentiality of the sale.

A better choice would be to use an experienced intermediary to contact and interface with potential buyers. (*This is something we will explore more extensively later in this report.*) A professional intermediary will provide the critical experience and knowledge in mergers and acquisitions. By providing access to a diverse network of potential buyers an experienced professional can help you fully develop the market for your business.

Q: After I find a buyer, what problems will I face?

A: Every sale is unique but there are key problem areas common to most transactions. For simplicity, we'll touch on only five here.

1. Negotiation

If there is one word that sums up what happens in a business sale, it's negotiation.

It is absolutely essential that your primary negotiator have at least the same level of sophistication as the buyer and his support staff. *(The vast majority of middle-market buyers today are professionals who spend all of their time identifying and acquiring businesses.)* Very few sellers have sophisticated negotiating skills or up-to-date information about these transactions. Even if they do, they are too close and too emotionally involved in the sale to be as effective as a third party professional.

We suggest that you do not use your attorney or CPA as your primary negotiator. Although skilled in their respective fields *(where they definitely should be involved)*, they are often less knowledgeable about the business aspects of the sale. They are also limited by professional restrictions and their relationship to the various parties in the deal. This is where an experienced third-party intermediary can make a tremendous contribution.

2. Legal Consideration

A great deal of legal scrutiny is required in any company sale. For example, the transaction may involve a sale of stock or assets. Service agreements such as non-compete and consulting contracts may be part of the purchase, as well. Purchase agreements with warrants, indemnifications, terms and conditions must be negotiated and carefully structured. It is, therefore, always important to select a legal firm experienced in the sale of businesses to provide this critical legal counsel, prepare these legal documents, and support your decisions.

3. Taxes

As an owner, your real results from the sale are directly dependent on the percentage of the sale price paid out in taxes. It is vital that your CPA, attorney and intermediary work to minimize your tax burden. Proper structuring of a sale can have a tremendous effect on your net cash from the sale. *(Analysis of the options and structure available should be completed long before a deci-*

sion to sell is made.)

4. Unions

What happens to a union during a sale can depend on whether the sale is of stock or assets. It may also be affected by the terms of the union contract, how the employees feel about the union, and the needs or requirements of both buyer and seller. It's a touchy area of negotiation and must be handled carefully. As a general rule, whether union or nonunion, good employees usually benefit from a change in ownership.

5. Costs

Legal fees may run up to \$15,000 on a \$1 million transaction and may total \$40,000 - \$50,000 on a \$4 - \$8 million sale. These figures should not deter you from retaining the best legal help you can get. Talk to several firms to determine their experience and aptitude in these kinds of transactions.

CPA fees tend to fall in the \$5,000 - \$15,000 range for all but the larger transactions. Your current CPA firm should be able to organize and establish the credibility of your financial data and also work effectively with the buyer's CPA. Intermediary fees range from about 10% on a smaller transaction down to 3% - 4% on a multimillion dollar sale. Example: on an average \$4 million sale, expect to pay professional fees of \$150,000.

A good intermediary earns these fees over and over again by professionally maintaining confidentiality, by getting the best price for the company and structuring the transaction to maximize the net cash proceeds you receive, to avoid post-closing problems, and most importantly completing the sale. *(Statistically, without the best professional advisors, only 1 in 3 mid-market transactions close as planned.)*

Before hiring an intermediary, find out on what the professional fees will be based: dollar value of stock, assets plus goodwill, etc. Also, find out if liabilities are included to reduce the dollar value of the transaction.

Be aware that the fees may be affected if real estate or leasing is involved in the transaction. *(Most experienced, professional intermediaries require initial retainers to cover up-front costs*

and a modest monthly fee during the project which typically will take 9 to 12 months.)

Q: How do I set a "price" for my company?

**Knowledgeable professionals recommend that owners
not try to establish a price themselves**

Aside from being too close to the company, few business owners have the experience, information, or tools to determine its value in the marketplace. You're better off calling in an outside evaluator-someone in the business of preparing companies for sale-who has current valuation experience and an understanding of recent market trends. Whoever sets the price range, the first step will be to determine the Adjusted Market Value of assets used in your business. This is done through a "recast" of the financial data to reflect market value of the company's assets.

The recast value differs from "book" value in that anything that would not be included in the sale of assets and liabilities is removed from the financial statement (*i.e. personal vehicles, owner notes, etc.*). What's left is adjusted to real market value-including inventory, accounts receivable, and equipment-providing a more accurate assessment of the company's hard asset value. For manufacturing companies, equipment appraisals will normally be required to structure financing. It is often advisable, therefore, to have a formal equipment appraisal completed before the business is put on the market. (*This appraisal should provide an estimate of market-value-in-place and is information often used to establish the proper insurance levels for a company..*)

Most experienced buyers and all bankers will also determine the liquidation value of the business. This valuation reference point helps the buyer assess the downside risks and is information that the seller should also have during negotiations. (*An in today's environment, it is information that is carefully assessed by financial institutions who may participate in the transaction.*)

Next the Income Statement is Recast. When prepared for tax reporting, the typical income statement lists historic expenses that may have a limited relationship to the future operation of the business, such as an owner vehicles, retirement plan, entertainment, or life insurance. In the recast statement, these items are removed to show the total cash flow available for taxes, debt service, and investment return. This adjusted income amount is then used to help determine the company's future earning-power and value.

Buyers will look at the adjusted income figures over a 3-5 year period. The average, or weighted-average income is then used to determine the historic Return On Investment. This information is used to analysis the potential future returns from exiting operations. Presently, experienced buyers are looking for a 30% - 35% return-on-equity. Although for strong stable business with a promising future, they may consider a return of 25% - 30% in exchange for reduced risk. *(This equity return should not be confused with the weight-average-cost of capital (WACC). The WACC maybe 15% to 25%.)*

As stated before, buyer are buying the future, but they want to base their purchase on the past performance of the company. The historic growth rate of the industry and the historic growth rate of the business are critical elements in any final determination of the expected return, since a buyer will only want to pay for a projection of the past trend. Therefore, it is extremely important that a seller document the basis for past trends and the reason for any changes in future expectations. It should be recognized that the buyer will discount growth projections that are not clearly indicated by the recent past performance of the business. **The price that will be acceptable to a buyer will be heavily effected by his/her confidence in the future growth of the company.**

The desired return on investment, adjusted for the impact of income growth, determines the price a qualified buyer will pay. In addition, the financing components in the transaction will be limited by the buyer's ability to communicate the underlying value of the assets of the business and the future earning capability of the business. Clearly, the recognition of these facts suggest that a consistent pattern of growth will help achieve both the highest possible selling price and the greatest percentage of cash at closing.

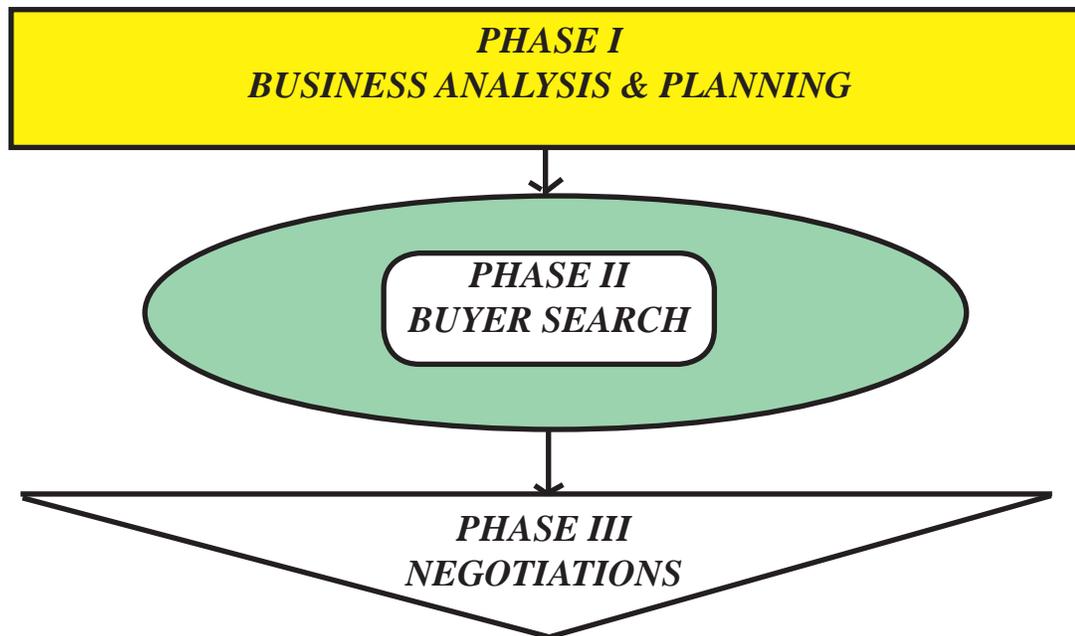
The unique difficulties in today's economy have impacted the prices of many businesses. As business activity improves, it will be crtically important for potential sellers to reposition their businesses to take advantage of the opportunities in the market place. The businesses that can convince buyer and financiers that the future should be consistently better than the recent past will be rewarded for their efforts.

Obviously, the relationships between income and net worth vary from business to business, affecting the price of each. A manufacturing firm, for example, might have more hard assets than a service firm, making it easier to transfer the manufacturing firm's income stream to a new owner. This allows for a higher purchase price even though the service business has a similar income.

Other risk factors affecting the purchase price may include: the length of time the company has been in business, the strength of the management team, and the mix of the customer base. The seller's willingness to accept a lower down payment and/or a longer payment period must also be taken into account. In some cases, this understanding and/or willingness of the seller may be the key to completing a transaction in a timely manner. *(Please remember: Things happen over time...some of these things may be out of a business owner's control, but they can impair business value non-the-less. If you are ready... and your business is ready...Don't Wait! If you do not believe this, just ask owners who missed the 1998 period and held their business for a number of years longer to complete an acceptable sale. The same thing is about to happen now for those business owners who decided to wait in 2007 or early 2008.)*

In addition, **it may be advantageous to avoid establishing an "asking price"**. In many cases a knowledgeable buyer will quickly establish the Investment Value that he or she would place on the business. This price could be based on special information that may not be known to the seller. It may also be possible to create a competitive bidding environment with as few as two buyers in order to maximum the selling price.

REAL WORLD VALUATION CHART



Q: What kind of payment should I expect? How much cash can I get ?

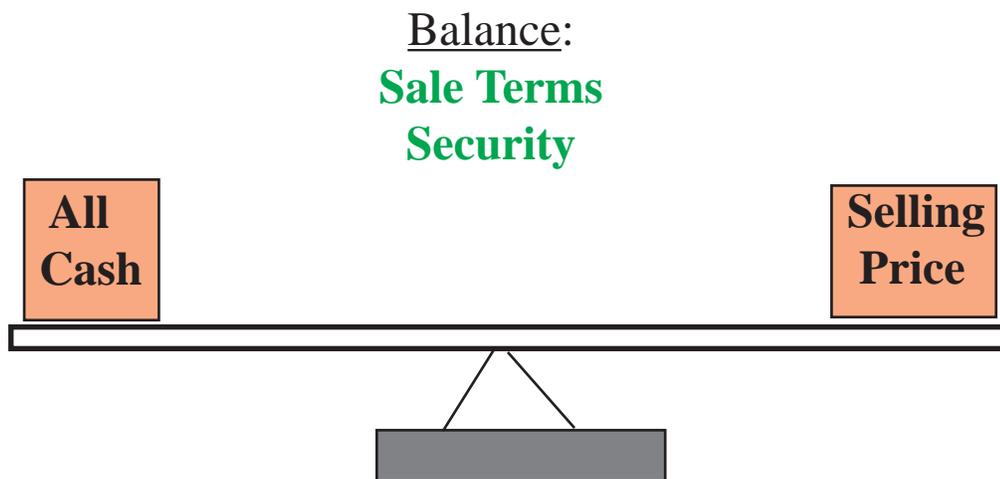
A: You might be able to get a cash payment but you will probably have to discount the purchase price about 20%. When the owner's note is properly collateralized, you're usually money ahead to take 40%-70% down and a note for the balance. Here are the terms for a couple of sample transactions:

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| 1. | Buyer down payment | 35% <i>(Cash to Seller)</i> |
| | Bank financing | 40% <i>(Cash to Seller)</i> |
| | Owner carry note | 25% |

The owner note may be amortized over ten years, but with a balloon payment at the end of five years. Interest at 5-year rates plus 1%. Payments of principal and interest monthly or quarterly. Note secured by second position on assets of company and personal guarantee of buyer.

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|----|--------------------|-----------------------------|
| 2. | Buyer down payment | 40% <i>(Cash to Seller)</i> |
| | Owner carry note | 60% |

Owner note amortized over ten years with a balloon payment at the end of seven years. Interest at 1 to 2 % over 5-year fixed rates, Interest only for first two years, then principal and interest paid quarterly for five years.



Q: You've talked about using an intermediary. Who should I use and how do I choose one?

A: We've already mentioned a couple of possibilities, such as your CPA and your attorney. We could also add your banker to that list.

But, as we said before, while they are all excellent resources to draw upon within their own areas of expertise, very few have the combination of knowledge, experience, or negotiating skills of the professional intermediary.

A business intermediary can oversee the entire sale, from initial appraisal through marketing, to final closing-with an eye for opportunities based on current market trends and past practices.

You should look for a business intermediary who is totally familiar with business sales in general and with the type of business you're selling. Choose your intermediary like you would choose a pilot-don't let a crop duster fly your airliner. Find one with the knowledge and experience to deal with your type and size of business.

A good intermediary should be adept at valuing businesses based on previous sales and current market conditions. (You would not have an operatins without a blood test...the same is true for the sale of your business. You need to develop the knowledge of: What Your Business is Worth..before you put it on the market. The intermediary can help in this area and should also be able to give you a realistic time frame for the sale.

Experience is vital, but the ability of the intermediary to understand the primary concerns for your business and your family are more important. Hire the intermediary with the same care that you would take with any key professional.

The right intermediary will be able to manage the transaction for you, or if you prefer simply provide needed support in some of all of the phases of the transaction. In a complex situation, it is critical to be able to discuss problems and concerns with a knowledgeable advisor. The members of the M & A Source network (www.MASource.org) not only have a depth of individual experience, but they have the advantage of being part of the largest independent network of mid-market professionals.

Before retaining any intermediary, a seller should find out:

- * Their background, what kind of work they've been doing.
- * How long have they been serving your size and type of business.
- * The relative success of their efforts.
- * Whether they understand your business in detail, not just on the surface.
- * Whether they are familiar with the tax and legal considerations of your sale.
- * How and where they will market your business.
- * What kind of industry contacts they have and whether they have any national or international affiliations that might give your sale broader exposure.
- * If they already have a buyer inventory appropriate for your business.

One important function of an intermediary is preserving the confidentiality of the sale. Although you don't want your sale to be so secret you limit your exposure, the proper level of confidentiality can help enhance your negotiating position and protect your ongoing company operation.

A intermediary can contact prospective buyers within your industry (*or even within your company*) to qualify them for interest and financial position, without revealing details or your identity. *A good intermediary will always require a nondisclosure agreement before releasing more than basic information to any potential buyer.*

Beyond the points mentioned, the intermediary will serve as your marketing and administrative manager for the entire sales process. The intermediary will coordinate efforts of the entire business sales team (*i.e. accountant, attorney, banker, etc.*) to assure an optimum, timely outcome.

A professional intermediary will set up a confidential, no charge, introductory meeting to review, at your convenience, the type of information in this report and to answer any other questions that you may have.

The intermediaries associated with the **M & A Source** network (www.masource.org) have a reputation for dedication and excellence. These professionals have the critical experience and the international support system to guide you through the sale process that is outlined below:

Phase I

Development of a Confidential Seller's Profile
Development of the Business Information Document

Distribution of a Confidential Seller's Profile
Buyer's completion of Confidentiality Agreement
Distribution of the Business Information Document
Establish buyer's ability to purchase business

Phase II

Facilities inspection by buyer(s)
Preliminary price negotiations
Deal structuring (*Agreement in Principle*)
Development of the Definitive Purchase Agreement

Phase III

Due diligence
Closing

There are over a hundred detailed steps in this sale process.

Every Single Detailed Step

should be executed carefully to achieve the optimal result!

Additional information and resources to help you save time and avoid costly mistakes can be found at:

www.MergerMentor.com