

Want to Sell Your Business: Start Planning Now

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Fact: Over 50% of today's businesses are owned by people over 55 years old. Most do not have an exit strategy and even fewer have enough money set aside to retire. These owners will have to sell their businesses to be able to afford to retire.

John Smith is a long time business owner here in Bellingham that wanted to sell his business. He owns a retail store and café. Like most small business owners he works long hours, provides exceptional customer service and makes a relatively good income. John was ready to hire a local realtor to help him sell his business. Before moving too quickly, we looked at the process of selling his business with the goal of maximizing his value or return on investment.

Deciding to Sell

Business owners sell their businesses for many reasons:

1. Retirement
2. Partnership dispute
3. Reduced interest in the business due to frustration or boredom
4. Illness or death of one of the owners
5. Sales and earnings have topped out because the company lacks working capital or the resources to grow
6. Losing money

Selling a business is different than selling anything else you own, because your business is a lifestyle as well. John had been a small business owner for over 26 years. The decision to sell his business was very emotional and many personal goals and issues also had to be dealt with. Know why you want to sell your business and what your goals will be after it sells.

Smart business owners carefully plan out their decision to sell their company. They recognize that selling a business requires proper preparation and not just a knee jerk reaction to external frustrations.

Preparing the Business for Sale

Most small businesses are operated with the objective to minimize tax liabilities. Unfortunately, these same operating techniques and accounting practices that minimize taxes also minimize the value of a business. Thus there is an inherent conflict with running the day to day aspects of a business and preparing it for sale. Plans to sell a business should be made three to five years in advance of the actual sale. This will allow the time necessary to make changes in accounting practices that will demonstrate a track record of maximum profits.

Other important aspects of packaging a business before selling include:

1. Have clean verifiable financial statements for the last three year

1. Stock only current inventory (reduce or eliminate dead, old or slow moving inventory)
2. Make the business physically appealing and clean
3. Have equipment be in good working order

The number one question business owners have is how much is my business worth. The only real answer is “What an educated, informed buyer is willing to pay.” However there is a solution that isn’t so arbitrary- getting a professional valuation report. A valuation report is usually prepared by a CPA, accountant or certified business broker. It helps eliminate the guesswork of determining a value of your business.

The final part of preparing your business for sale is to develop a business presentation package:

1. A history of the business
2. A description of how the business operates
3. A description of the facilities
4. A discussion of the suppliers
5. A review of marketing practices
6. An analysis of the competition
7. A review of personnel, organizational chart, job descriptions, pay rates and benefits
8. Identification of all the owners
9. Discussion of insurance coverage
10. Discussion of any pending legal matters or contingency liabilities
11. Last 3-5 years financial statements

Finding a Buyer

Print Advertising

Business opportunity ads in local newspapers are one way to get the word out that your business is for sale. Ads typically describe the business in a few lines and list a phone number or post office box for inquires. Most people will be scared away from a post office box, while a phone number isn’t as confidential. Even so, this approach maintains confidentiality and doesn’t openly tell everyone that your business is for sale.

Trade Sources

Trade associations, newsletters and publications are also good sources of advertising your business for sale. Every industry has a trade association; some are national, statewide or local. A classified ad in their monthly newsletter may be the source of that treasured buyer. Often key people or suppliers within an industry know which business is for sale and may be even aware of potential buyers. The down side of trade associations is that it presumes that the best or only buyer for your business is someone already in your industry. Statistics show, however, that most buyers of small businesses are not currently in that specific industry.

Intermediaries

Business intermediaries can be divided into two groups: business brokers and merger and acquisition specialists. Business brokers generally handle small and medium sized business sales, while merger and acquisition specialists handle large business sales. Each of these intermediaries will typically ask for a 180-day exclusive contract to sell your business.

Business brokers are of two types: professional certified business brokers whose primary business is brokering business sales and those paraprofessionals, like real estate agents, that sell other things as well. Business brokers charge a fee usually up to 10% of the purchase price for their services. The seller usually pays this fee.

An experienced business broker will help the buyer in preparing the presentation package, pricing the business (valuation report), setting the terms, professionally marketing the business, screening potential buyers, negotiating and evaluating the offers, and making certain that correct legal steps are taken. Working with a good business broker can save the buyer considerable time and effort in selling your business.

Hiring an Intermediary

Hiring the right business broker is critical to the selling process. Interview prospective brokers and their associates. Often the broker is not the one actively representing you to prospective buyers. Inquire about their credentials, training and years in business. Ask for references and check them out. Choose someone that you can trust to represent your best interests. You want a broker to be working for you not the buyer.

Pricing the Business

Determining the value of a business is the most difficult part of the buy-sell transaction process. It is fraught with differences in opinion as to the worth of the business. Rarely do buyers and sellers share the same perspective. Each party has their own rationale, which may be based on logic and or emotions. For the transaction to come to fruition, both parties need to come to agreement and understand how this agreement was derived.

Factors that determine value

While there are many factors that impact the value of a business, six of the key factors are:

1. Recent profit history
2. General condition of the company
3. Market demand for that type of business
4. Economic conditions
5. Ability to transfer goodwill or other intangibles to the new owner
6. Future profit potential

These key factors are impacted by other issues that help determine a fair market price:

- Special circumstances of the buyer or seller
- Trade off between cash and terms
- Tax consequences for the buyer and seller, which determines how the offer is structured

Rule of Thumb Formulas

The only rule of thumb regarding valuing a business is that there is no rule of thumb. Rules of thumb do not address the unique aspects of your business. No two businesses are the same, so don't rely on "one size fits all" formulas.

However rules of thumb do create a quick reference point to see if the valuation is in the "ballpark." A good reference book for this information is: *Handbook of Small Business Valuation Formulas and Rules of Thumb* published by Valuation Press.

Valuation Methods

There are numerous methods of determining a value for your business. Some of the common methods of valuation are:

- Balance Sheet Methods: Book Value, Adjusted Book Value and Liquidation or Bankruptcy Value
- Income Statement Method: Discounted Future Cash Flow

Each of these methods is complex and beyond the scope of this article. These methods require the help of an accountant, business broker, or management consultant. Obviously, it also requires accurate financial statements from the seller as well.

In conclusion, if you are thinking about selling your business, plan ahead, package your business for maximizing its value and consult with professionals to guide you in the process. John is still in the process of preparing his business for sale, only now he understands the process and where he's going.