Look What I’ve Built, Now What Do I Do?

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Today we will discuss:

1. Basics of the business valuation process: familiarization of the process
2. How to prepare yourself and your business for your eventual sale or succession to another party, related or unrelated
3. The how-tos of successfully transitioning to the new owners
We Have a Choice
Business Valuation

1. Not an exact science
2. One size doesn’t fit all
3. Shouldn’t be done by unqualified people
4. Mistakes are easy to make
5. In the end the value is only an estimate; you will need to have an expert negotiate for you
Basic Valuation Methods

1. Income approach: discount or capitalization rates
2. Asset based model
3. Market model
4. Beginning assumptions
   - What is the purpose?
   - Financial analysis
   - Economic Conditions
Income Approach

1. Value is derived from analyzing financial records
2. Generally preferred model for service businesses
3. Basically determines value from discounting or applying cap rates to historical cash flows
Other methods

1. Asset based model: only used for companies with a lot of assets

2. Market approach: Uses comparative values to other businesses that are similar in service and product mix. Generally applies a multiple to sales or ROI or another financial measure
Preparing Your Business for Selling

1. Proper preparation will add value to your business
2. Most common mistake made by small professional service business owners
3. Will need 3-5 years to prepare
Key Performance Indicators

1. Cash Flow history: 5-7 years
2. Principal’s salary with all perks
3. Client burn rate or retention history
4. Competitive position of the business
   - Use of technology
   - Demonstrated skill of consulting team
   - Age of principals
Common Shortcomings

1. Poor financial records
2. Misuse of tax deductions
3. Not accounting for entitlements
4. Lack of business productivity measures
5. Not a student of your business
6. Intentionally understating financial performance
Common Shortcomings-cont’d

1. Lack of adequate cash in company; reliance on operating loans
2. High employee turnover rates
3. Lack of adequate earning’s history dramatically impairs enterprise value
4. Lack of company growth in clients and revenues
Common Shortcomings-cont’d

1. Excessive AR losses
2. Weak or non-existant legal contracts for service
3. Weak collection practices
4. Record of lawsuits against company
5. Unpaid Federal Tax and FICA deposits
Keep your charts handy
How to Prepare for Business Transition

1. Develop a 5 year plan for the business and yourself
2. Start process before you are ready to slow down, know where your business is on the business life cycle chart?
Business and Personal Life Cycles

Start-Up

Growth

Maturity

Renewal

Decline

Personal Life Cycle

Business Life Cycle
How to Prepare for Business Transition

1. You will be shortchanging your take from the sale if you have already decelerated before putting the business up for sale. Once your business starts downhill, it is hard to reverse that trend.
How to Prepare for Business Transition

1. Recognize that you may have to work for your buyer for up to 3 years after you sell to ensure that your clients feel comfortable with the new buyers.

2. Seek and find a buyer while you still want to hit it hard.
How to Prepare for Business Transition

1. Earn-outs are common, be prepared for discounts for sales under projections, however, negotiate a deal to share the ups if you are over.

2. Beware of partial buyouts with you carrying the paper; you are not a bank!
Best Practices

1. Assemble a competent team of advisors to assist you in this journey; it is too much to do alone!

2. Team needs to include your CPA, a business valuation specialist, a good attorney that will listen to you, your financial planner and a quarterback to the team.
Now, Get to Work!

Develop your vision and strategic imperatives for the transition. The who, what, when, where and why, at least 5 years prior to when you want to be able to decelerate.
Now Get to Work!

1. With your business valuation specialist, determine what improvements need to be made to maximize value from the business.

2. Develop action plan with team quarterback, to ensure things are getting done, after all, you still have to do the work!
Targets and Metrics

1. Working capital at 15% of annual revenues
2. Gross profit on cash revenues of at least 20%
3. Charge offs less than 2% of annual sales
4. Annual revenue growth of at least 5%
Targets and Metrics

1. Account Receivables 90% less than 60 days
2. Legal documents approved by attorney
3. Documented policies and procedures, need to demostate you are system driven
Targets and Metrics

1. Keep accounting up to date using acceptable software
2. Crank out key performance measures on a monthly basis to show that you are in control of your business
Summary

1. You can put lipstick on a pig, but remember you still have a pig!

2. Be a student of this process, study, talk to peers that have been through this process, especially those that have failed.

3. Build a financial nest egg; there will be bumps or craters in the road.
Is Your Business Ready?
Question & Answer
Thank You for Joining Me!

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