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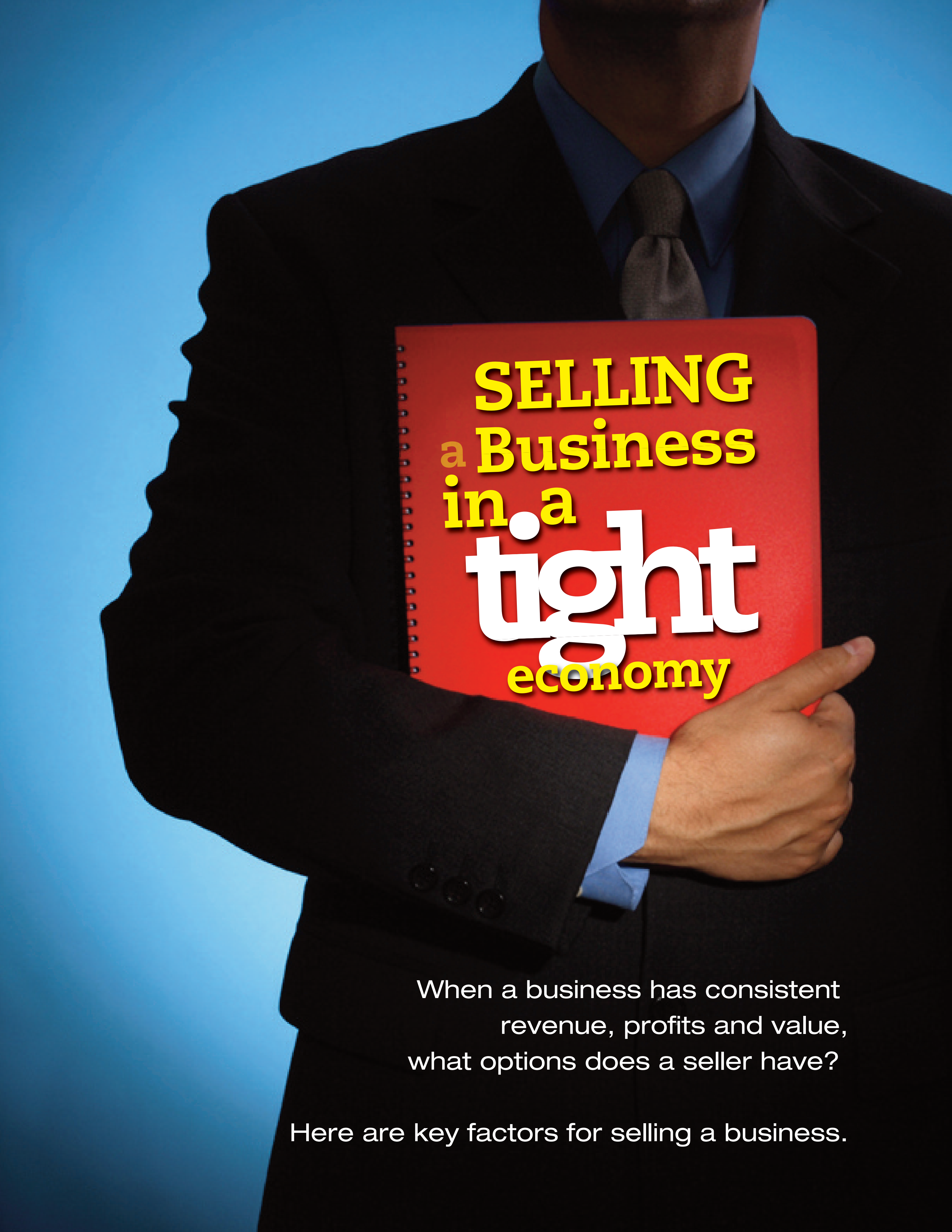


SELLING a Business in a tight economy

When a business has consistent revenue, profits and value, what options does a seller have?

Here are key factors for selling a business.

BY MATT COLETTA

Buyers are more educated than ever these days, and they are not taking risks. The current marketplace is such that there is a healthy pool of buyers with impressive backgrounds and liquid funds looking to purchase quality businesses. Buyers are coming out of corporate America and looking to purchase businesses by using their savings or retirement funds through various programs as a source of down payment.

Younger Baby Boomers (mid 40's—50's) are also looking to fulfill their dream of owning and operating their own business prior to reaching retirement age. The key is in understanding what motivates buyers in today's market in order to successfully sell your business.

determining the multiple for your business

Buyers purchase "cash flow" when they purchase a business. Cash flow, also know as discretionary earnings, is the net income plus certain acceptable owner benefits or "perks." Businesses with cash flow and "transferable value" are in demand in this economic environment. Buyers are willing to pay a multiple of cash flow which is determined by the type of industry, years in business, key employees being in place, condition of the equipment and facility, lease terms and the type of finance available. There are many other factors that go into determining this multiple and therefore the value of a business. An experienced Certified Business Broker can assist you in determining the cash flow, multiple and ultimately the correct value of the business.

If the business does not have traceable, verifiable cash flow, then it needs to be sold as a Sale of Assets in Place, which yields a lower value. Although the buyer pool for these businesses is less, there is still a demand for these assets in place by individuals willing to take a risk to turn the business around. The value is ultimately determine by the market place so it is important to highlight the benefits.

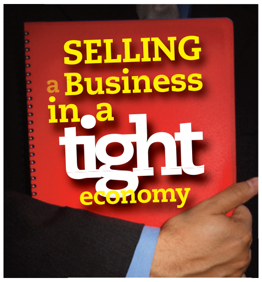
packaging your business for sale

A second key item to selling a business is in packaging it correctly. Buyers need and demand information. They need to know everything about the business to see if it will meet their needs as they are typically putting down a significant portion of their life savings at risk. It is important to package the business so that the features and benefits are outlined clearly. It is also important to clearly outline the cash flow of the business and all the add-backs. The bottom line is the bottom line, so it is important to explain how the cash flow was derived. Buyers will typically not move forward unless they are comfortable with this analysis. In addition, if a buyer does not feel comfortable with a business's transferable value which includes policy and procedures, whether or not key employees are in place, if the business has growth opportunities and a sturdy marketing plan, if the assets and systems needed to move forward are in place and in good condition, etc., then the buyer will most likely not be willing to take the risk and the business will not sell.

how buyers can finance the purchase

The last key element is how a buyer finances a business purchase. The choices are limited. Typically there are three methods:

All Cash. This is not common. If a buyer is willing to pay all cash, then the buyer will expect a discount in



the purchase price since price is a function of terms.

SBA Finance. There is a big misconception on how financing with a Small Business Administration loan works. First, these loans are among the highest risk loans for a bank that typically funds the loans using a SBA guarantee. In today's economic environment, these loans are extremely difficult to obtain. The banks will only consider what is on the selling company's tax returns. The tax returns must show consistent year-after-year gross revenue and profitability in order to assure the bank that the cash flow is there to cover the debt service. The bank and SBA will also require that the buyer have direct industry experience, good credit, ample reserves and, in most situations, additional collateral to secure the loan.

In some cases, the bank and SBA may require that the seller carry a portion of the purchase price in second position, sometimes with no payments for 3-5 years. This depends on the verifiable cash flow available to cover the debt service. These loans are typically leveraged with 10-25% down, and therefore the payments can be high for the buyer. For some transactions, this may be a viable option, but as you can see, it can be challenging to meet some of the requirements.

Seller Finance. This has been the most common method of financing in the last five years. The advantage with seller finance is

Some Of The Lingo

Bulk Sale Requirements: A law that regulates the transfer of business assets so that business owners cannot dispose of assets in order to avoid creditors. If a business owner wants to conduct a bulk sale of business assets—that is, get rid of all or most of its inventory, merchandise, or equipment—the business owner must give written notice to creditors and, in some states, publish and record a notice of the sale. This is also in place to protect the buyer.

Discretionary Earnings: This is the cash flow of the business after adding back certain, traceable, non-business related expenses to the net income.

Multiple: A multiple is derived from a number of business, industry, market, and owner pref-

case in eg. point

Long-Standing Family Business Thinks Out Of The Box

Two partners owned a 50-year-old box manufacturing business that their fathers started. The partners after many years of running the business wanted to sell. They had lost a large long-term customer and the revenue had decreased. The business still had a reputable name, long-term employees in place and a working facility. After much discussion, the partners decided to sell. Their accountant referred them to our firm. We went in and evaluated their business given their situation at no cost and gave them an opinion of value. The value took everything into consideration.

The sellers thought their business was worth more but we explained to them that the recent lower cash flow was bringing down the value. We also explained that financing would be difficult to obtain which our lender confirmed. We agreed on a starting selling price, and after discussing the benefits of seller finance and how we would structure it to secure their position, they agreed to offer seller finance subject to approving the buyer's qualifications and credit worthiness. We created a detailed package on the business highlighting the features and benefits including the 50-year history, long-term employees in place, financial analysis, among other key factors.

We went to market and started identifying potential buyers. We learned after discussing the business with several buyers, that this would not be an easy business to sell. Most buyers agreed that the business had an excellent reputation, employees and facility but they were concerned with the drop in revenue as erences factors. The multiplier is used to convert a single-point business economic benefit into the business value.

Sale of Assets In Place: When a business lacks verifiable cash flow, it can be sold as a Sale of Assets in Place. The business may have value for certain assets that are already in place and ready to be used by a potential buyer. The market place and what a willing and able buyer is willing to pay typically determines the value.

Transferrable Value: The value of a business going forward. Tangible benefits such as policy and procedures, key employees that are in place, growth opportunities for the business, a marketing plan, and any other systems that are in good condition that add value to the business.

that the seller will be able to set the requirements. Seller finance typically involves a buyer being screened both financially and work-experience wise. This kind of transaction typically begins with requiring 40-50% down and is negotiated from there. When a buyer puts 40-50% down and a seller carries 50-60%, this creates an even playing field. The buyer has "skin" in the game as well as the seller. It is crucial to set up seller finance correctly upfront and put mechanisms in place to reduce the probability of a problem down the road. Again, this is where a Certified Business Broker is key to assisting in this process as well as managing the entire transaction from beginning to end.

Selling a business is an extremely complex process, so it is important to work with a broker who understands the dynamics of selling a business in this current economic environment. No two deals are ever alike. Selling a business can be just as much of an art as a science. When you work with someone who has the experience to analyze the specific situation and develop a custom plan to price, package, market and structure a transaction, the chances of selling a business successfully increase tenfold. •

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a result of losing a large customer. Remember, the majority of buyers purchase cash flow and they must feel comfortable with the company's transferable value.

The sellers had no formal marketing plan in place and did not do much to generate new business. We suggested to the sellers that they immediately focus on trying to generate new customers in order to show that new business was attainable if someone put in the time and effort to go out and do so. The facility had the capacity to handle more business; someone just needed to generate it. After a short period of time, the company started obtaining a handful of new customers. The revenue began to increase and it became clear that the company could rebound.

We re-priced the business and marketed it using our wide range of company resources. It took some time and speaking to several buyers to discuss the features and benefits, but we eventually found a buyer who saw the transferable value and potential to turn this business around. We had several meetings with the buyer. Once he completed his due diligence, we opened escrow to comply with the bulk sale requirements and complete the transaction. The buyer said one of the main reasons he considered this business was the fact that the seller was willing to finance a portion of the transaction. This made him feel comfortable with the fact that the seller had confidence with the business going forward. The transaction closed and after training was completed we all celebrated.

The sellers were happy, as they were now able to retire and focus on their other activities. The buyer was happy, as they saw many opportunities to expand the business and had already implemented some of them. The buyer indicated that he was glad he purchased the business, but he probably would not have gone forward unless the sellers agreed to carry the note. Everyone was happy and after several months of operating the business, the buyer has increased the revenue substantially and has indicated that he will most likely pay off the note sometime this year. •