A Simple Introduction to

Selling Your Business

How to prepare your business to get the results you want

Calhoun

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Introduction

You've worked hard to build your business. We understand that what happens to it is important to you. For more than 100 years, Calhoun Companies has served as matchmaker for buyers and sellers, guiding both into the next phases of their lives. We focus on small- to mid-sized businesses, helping them leverage their assets and realize their goals through business brokerage, commercial real estate, mergers and acquisitions, and business valuation services.

In this book, we bring you a summary of what we've learned over the last century. It contains everything you need to know about selling your business, from initial preparation all the way to life after the sale. Our hope is that this information will help you set your business up for a successful sale, and usher you smoothly into your next adventure.

This guide is based on real world facts and how they impact the sale of businesses. It is not lengthy. I could have rambled on, but we all know business owners have enough pressing demands on their time. Instead, this guide was written to be both easily accessible and digestible. Every business owner needs these insights, and now every business owner can have them.

Selling your business can be one of the most significant and complex financial transactions you will ever experience. Our knowledgeable professionals possess the perfect combination of expertise and care that you and your business deserve, and are ready to talk when the time is right for you.

This guide has been written by Andy Kocemba, President of Calhoun Companies.

Chapter 1: When is it Time to Sell My Business?

"How can I beat the market?" It's a common question these days, whether referring to stocks, home sales, or the sale of any other item or commodity. I often get the same question regarding the sale of businesses. Owners want to know if now is the time for them to beat the market and maximize the value of their business.

The answer, however, is that there is much more that contributes to selling for top dollar than just timing the market. A market may be positive and riding high, but an unhealthy business will still be difficult to sell.

Here are two areas to analyze as you contemplate selling your business.

Business Health: What are your financial trends? Your business will always sell for more if the numbers are trending up than if they show a downturn. Many owners have a tendency to hold their business too long rather than opting to "Sell High."

How about your employees and infrastructure? Are they happy and on-board? Is everything humming along? Your business will sell for more if there are no major issues with employees and if the staff is committed. The same can be said for client and customer relationships.

Are your financials positioned and showing profit? If you have decided you are mentally and emotionally ready, the next item to consider is the state of your company from a financial perspective. First, are you profitable? Buyers want to purchase a company that will return their investment. The more profitable you are, the more your company is worth.

Secondly, do your financials show that full profitability? It is common practice for business owners to minimize their profitability for tax planning purposes, but in the years leading up to a sale, it's good to have your profits maximized on your statements, clear as day. This will make it obvious to buyers why they should pay a premium for your business. Also, make sure those financial statements are clean and organized.

Is your house in order? Lastly, make sure your business is ready to hand over to a new owner. Do you have your processes well documented? Is your operation well organized? The quicker a buyer can understand your operation and picture himself in the corner office, the more confident they will be in buying the company and paying top dollar.

Personal Commitment: How do you feel about your business? Do you have the energy and commitment to keep it going strong? Business owners often underestimate the time needed to sell their business, and in the end, "run out of gas." The business suffers and ultimately, the sale price goes down. To maximize the value of your business, it is important that you are able to give it your all until the day you hand over the keys.

Are you ready? Can you picture your life without your business? What are you going to do with your time? The reality of business valuations is that if you continue to run your company for approximately three to five more years, you will earn near the full sale price that anyone would pay today. If your response to that is, "That's crazy, why wouldn't I just work three to five more years?" that's a pretty good indicator you aren't quite ready to move on.

The health of your business and your willingness to put in the effort to keep it sharp have a much greater effect on value than the outside forces of the overall market. If your financial trends are strong, but you feel your energy waning, now might be the perfect time to sell and get the highest price, regardless of what the business section of the newspaper might tell you. If the financial performance is down, but you have the commitment to grow the numbers, you will likely get a higher price in the future. Take a look at your business's health and your own personal commitment before deciding when it is time to sell your business.

Chapter 2: Getting the Biggest Buck for Your Business

Imagine two businesses: Owner A works long hours and doesn't make much money. He hasn't had a vacation in years, and doesn't really stand out in the market place. Owner B runs a highly profitable company and takes three vacations a year. Her staff excels while she's home or away. Her company has distinct processes and a reputation as being the best in the business. All else equal, for which business would you pay a higher price?

At some point during every business owner's career, the question of business valuation comes to mind. Whether you are nearing the point of selling your company, or are in the earlier stages of building your business, there are three main value drivers you need to be aware of:

Profitability/Earnings (Cash is King!): The first thing anyone considering buying your business will look at is your profitability. Is your business making money? By and large, this is what buyers want, and the general value of your business is going to be based on a multiple of earnings. The higher the profitability, the higher the value of your business. Make sure your financials show the profits as well. It's not uncommon for business owners to take profits from the company in many ways, just make sure the profits are all on the books and you can clearly show a potential buyer where all the money goes.

The Intangibles: Items like infrastructure, intellectual property, brand and strategic fit can have a profound impact on how a buyer values your business as they impact the multiple a buyer will apply to earnings to determine value. Can the business run while the owner is away? Do you own a patented product? Are you the most established and reputable brand in the market? The more you can answer "yes" to questions like these, the higher the multiple a buyer will use. Conversely, as these items are absent, multiples decrease and values drop. As you become more aware of these items in your business, pay additional attention to how well they would transfer to a new owner. These are the things for which a buyer would pay a premium price.

Real Estate, Inventory, & Cash, Oh My!: The market value of these three, plus any other balance sheet items that would transfer with the business, are added to the multiple of earnings value. These are assets that in and of themselves are not crucial to generation of earnings, and thus don't factor in to the multiple of earnings component. They are simply additional assets being sold with the business.

Chapter 2: Continued...

Simply put, here is how you calculate the value of your business:

Profitability/Earnings
× Industry Multiplier
+ Certain Assets

$ Business Value

Whether you are a business owner who will be selling your company in the next few years, or a business owner growing with an eye on the future, building upon and improving these distinct areas will directly increase the value of your company come the day you decide to sell.

Chapter 3: Who is the Best Buyer?

If you anticipate selling your business in the next few years, you've probably already begun to imagine who the buyer will be. You might hear stories of your former business-owner friends and who they sold to, or catch a news story highlighting a successful transition, but still wonder what the best path for you is as you exit your business. It is important to understand all options available. Here is a list of the main types of buyers you will encounter, and the pros and cons that come with each.

Family Member: This is often the first transition option that will come to a business owner's mind. He or she will consider their children as the ones to take over the family business. While there are inherent benefits such as familiarity with the business and an elevated level of trust, one must take a deep look at whether the child is a good fit to run the business, and if they in fact want to run the business. There is also heightened risk with a family transition in the event the business should falter. Not only might the seller forego any future payments he may be due, but there is the added damage that may have been done to family relationships. Remember, family is more important than business! Because of the far-reaching impact this buyer type could have, we will take a closer look at this option in the next chapter.

Synergistic Buyer: This is another company that would acquire you. They might be a direct competitor, or perhaps they are in a similar industry and are looking to enter yours. Either way, they have synergies to be gained by acquiring you, which make the deal more beneficial to them than to other buyers. For example, if they were to acquire you and utilize the components of their own business already in place, they might be able to eliminate a lot of your current office expenses, combine manufacturing facilities, etc. This makes the business more profitable to them. As a result, they might value your business higher than other buyers. A negative is that they might make significant reductions to your staff, and if you value your employee's jobs going forward, this might not be the best buyer for you.

Financial Buyer: This buyer looks at your business from an investment perspective. They might call themselves a Private Equity Group or a Family Office, but either way, they have a timeframe of ownership and a return on investment in mind. Pros: They have the money and expertise behind them to grow your business to the next level. Often, they might make a partial payment to you up front and keep you on board, allowing you to benefit

Chapter 3: Continued...

from their growth efforts when they sell the company or buy you out completely years later. Cons: You will likely be asked to stay on as an employee for at least a year, something you probably aren't used to.

Your Employees: At first glance, this might seem to be a good fit. They know your business, have proven their loyalty, and you can trust them. There are pitfalls to be aware of, however. Do they have the money to give you the down payment you are looking for? Often employees don't have the financial means to buy your business. Do they have the skills to run the company? The character traits that make good employees often don't translate to being good owners.

Individual Buyer: While perhaps not the first buyer type that comes to mind, the individual buyer might just be the best fit for you and your business. This buyer is either a serial entrepreneur, or someone leaving corporate America to chase their dream of owning a business. If they have savings and the ability to get financing, you will get the cash you need upon closing the sale. Because of their lack of specific industry experience, they value what you have built and will pay a premium price to ensure your commitment to a smooth and successful transition.

There's not one single buyer type that is best. All can bring good things, but also drawbacks to a business transition. Knowing the different options and their pros and cons can help you better clarify your goals as you exit your business, and prepare you for responding as different buyers make you offers.

Chapter 4: Is Family Succession Right for Your Business?

As we mentioned in the previous chapter, transitioning your business to a family member is a possibility that could be a great fit or a terrible fit, depending on the factors involved. It seems just about every week there is a different seminar, webinar, or blog that comes through my email inbox pertaining to succession planning. It's become a bit of a buzzword these days. The experts want to share how to best transition your business to the next generation. But, how do you know if transferring the business to your children is in your best interest, their best interest, or the company's best interest? Here are the top three reasons why you may want to look to an outside buyer when it becomes time to transition out of your company.

Interests: Simply put, your child may not want to run your company. When you look at society today, it seems more kids opt to go a different direction than their parents, rather than follow in their footsteps. Don't be surprised if the same can be said for your family. Most parents can agree that they want their children to lead happy, fulfilling lives. Don't push them into a career they would rather not pursue.

Skills: This one may be a little trickier to discern. A son or daughter may express interest in the business, but do they have the technical skills, business acumen, and leadership ability to take the reins of the company? You know the hours, dedication, and sacrifice it takes to grow and run a business. Do you see that ability in your children? Also, keep in mind that the child that expresses interest may not have the skills, while a sibling who has not previously expressed any interest may in fact be the ideal heir.

Money: One of the primary motivations in selling a business is to move on to something different. Whether it is retirement or the next business opportunity, that next endeavor will take money, meaning you are likely looking to take some of the hard-earned equity you have in your business off the table. Outside buyers will usually have much stronger abilities to bring cash to a transaction and into your pocket. Conversely, putting together a deal with one of your children usually involves little to no cash at closing, which leaves you with next to nothing after closing, and saddles them with enormous debt obligations. Depending on how greatly they possess the above-mentioned interests and skills, they may never be able to pay, and you will be left taking back a broken business.

Chapter 4: Continued...

Family business can be a great thing, but it's best to proceed with caution. There are risks to consider that you wouldn't necessarily face in dealing with an outside buyer. Family is one of the most important things in life, and it would be a shame if something like business got in the way.

Chapter 5: Selling is a Team Activity

Growing up, I learned a lot about home improvement from my dad, and today, I am an avid "do-it-yourselfer." The primary reason I can be successful in my home projects is that I know my limits. My dad always said, "If it's behind the walls, I don't touch it." Meaning, he knew when to call the plumber or the electrician. I have learned to do that as well.

The same can be said about the process of selling your business. To maximize the value of your business, make the process smooth, and keep the business healthy until it is handed over, you must bring in your team of experts. You have grown your business by being an expert in your field, and have likely relied on a team of experts from other fields. When you are beginning to sell your company, it is time to draw them in even closer.

Here are the critical team members you will want to include as you sell your business. Keep in mind, the team will function best with one quarterback or captain. It doesn't necessarily matter who that is, and it could even be you, but make sure it is known who is leading the team.

Business Broker/M&A Advisor: This is often the team member who gets the ball rolling. They will be the one who brings the business to the marketplace in a presentable fashion, including establishing value and beginning the search for a buyer. They are matchmakers and can be a good quarterback choice to guide the deal through to a successful closing.

Accountant: Most likely, you have been working with this person for years, and they will continue to be instrumental in successfully selling your business. Clean and organized financial statements both maximize the value of your business and earn the trust of potential buyers. Buyers want to know that "the house is in order."

Attorney: A good transaction attorney will be able to analyze documents on your behalf, looking out for your best interests. Make sure they have experience in business transactions.

Financial Advisor: Hopefully you have built your business well, and upon closing the transaction, you will have a sizable amount of money you need to put somewhere. A good financial planner can help you come up with the plan best suited for you and your family. Also, along with your accountant, they can help you plan for the tax ramifications of the sale, ensuring you get to keep as much money as possible.

Something to remember regarding all members of your team: make sure they are deal-makers, not deal-killers. You are the boss and you have decided to sell your business. Make sure each team member is aligned with your mission and goals. Help yourself by asking for help from your team. Recognize your limits when you are entering the "behind the walls" phase. It will lead you to a successful transaction.

Chapter 6: Choosing a Business Broker

Now is the time. From humble beginnings, you've grown your business to the success it is today. It has supported you and your family, but now it is time to sell and move on to the next chapter in life. While you may be tempted to sell your business on your own, hiring a proven business broker can simplify the process and earn you a higher sale price. But, how do you hire the right broker?

During a phone conversation or an initial meeting, try to get a feel for how a broker stacks up in each of the following categories:

Experience: Going with an experienced company and broker is crucial. How long has the company been in business? How many deals do they close each year? Questions like these will ensure they do quality work, have ethical processes in place, and can represent you well. A broker that has sold businesses like yours in the past can anticipate challenges and know how to guide a deal to closing. However, a broker newer to the industry can bring energy and motivation in representing you, and if he has a strong company behind him, he can be just as effective as a broker who has been in the business for 20 years.

Credentials: First and foremost, make sure your broker is properly licensed. From there, find out what industry organizations (the International Business Brokers Association and M&A Source for example), local chambers, and other groups they belong to. While licensing is the main required credential, the others can give insight as to their level of expertise and involvement in the business community.

Leadership: Are they well respected and connected in the community? Do they give back? Are they connected to attorneys, accountants, bankers, and other professionals who might all play a role in getting your business sold? Ask those advisors what business brokers they have worked with in the past. I'm sure they have opinions.

Communication: At the beginning of the process, make sure your broker is open, honest, and responsive to you, and is willing to take the time to understand you, your company, and your goals. Further along in the process, make sure the broker plans to communicate with you in a way that meets your expectations. Selling a business can take time, and there may not be any news on a week to week basis. Make sure there is a clear understanding between you and the broker as to how and when communication will take place.

Being a Team Player: As we discussed in the previous chapter, selling a business is a team game. Make sure that the broker you choose is not overly controlling, and can work well with others. They should be more than open to having your attorney, accountant, and other professional advisors involved in the sale of your business. A good broker will not try to shut out others so that he can control the situation, but will recognize the importance each plays in the process, and will seek to include all while guiding the business to a successful sale. Balance is key, however, as you want him to be assertive enough to keep the process moving forward.

That Feeling: You will have more fun working with someone you like and respect. Look for character and personality traits you value and appreciate. There are as many different types of business brokers as there are different types of people out there. Find one you feel comfortable with and confident in.

Chapter 7: Maintaining Confidentiality

From the onset, one of the primary concerns of any business owner interested in selling is how to keep their actions confidential. They might say, “I don’t want my customers to know I’m thinking of selling,” or, “my employees can’t know what I’m planning.” While a business owner ultimately must be prepared for the word to hit the street, there are ways to manage the sale to maintain confidentiality as long as possible.

Blind Advertising: Any advertising on a business that is for sale should be “blind advertising.” The goal of blind advertising is always to drive inquiries, not to reveal the business. Ads should be written generically, stating the industry, approximate size of the business, and possibly general location, but nothing that would lead anyone to know specifically what business is for sale. Depending on the industry and number of similar businesses in the geographic area, some of these ads can be more specific than others, but always ask yourself, “Can someone tell who I am based on this ad?”

Confidentiality Agreements and Buyer Qualification: Once you are attracting the attention of potential buyers, it is imperative they sign a legally approved confidentiality agreement before any of your information is released to them. If your sale is being managed by a broker or M&A professional, this form will be signed before they even reveal the name of your company. This is also the time a buyer will be qualified to see if they have the means and the ability to buy your business. If not, there is no need to release any confidential information to them.

Be Ready to Answer: Ultimately, customers and employees may start asking you if the business is for sale. This question may be innocent enough, so it is best to always have an answer ready for anyone that brings up the subject. My favorite strategy is to play it off in a lighthearted fashion. Responses such as, “Everything’s for sale for the right price,” or, “Did you bring your checkbook?” defuse the situation quickly, and put the pressure back on the asker of the question to reveal their motives.

Manage the Process: A signed purchase agreement doesn’t mean the need for confidentiality is over. Make sure you and your buyer have a clear understanding of when employees will be told of the sale. While some key employees may need to be drawn into the process earlier on, it is generally best to wait as long as possible to tell employees a business is being sold, often sharing the news after closing the transaction. Until

Chapter 7: Continued...

ownership is officially transferred, you never know what might happen and a deal might fall apart. In that case, it is best employees and customers not be aware. Remember that maintaining confidentiality through the selling process is important, but it is not an all-or-nothing scenario.

These tips can help you maintain confidentiality by knowing what to share and say, and when. Brokers and M&A professionals can guide you through this process and lead you to the best results.

Chapter 8: Speeding Up the Sale

"How long will it take to sell my business?" is one of the many questions I get asked about the process of selling a business, I always joke that this is the one question I can't answer. There are just too many factors that come into play. While it may be impossible for me to say for certain how long it would take to sell your business, there are ways to speed up the process.

Reasonably Aggressive Pricing: Pricing is one of the most important factors in a quick sale, and working with an experienced broker is one of the most important factors in making sure your business is priced correctly. While it might be tempting to think that the lower you price your business the faster it will sell, this isn't always the case. There is a point at which a business can be priced too low relative to its cash flow, causing potential buyers to become suspicious of why you are selling. They might get the impression that you are trying to dump the business and that you might know something they don't. Buyers may be looking for a good deal, but they also expect to pay a reasonable price for a good business. An experienced broker can help you identify the realistic price range within which your business would sell, and if speed of sale is one of your primary goals, consider going to market at the low end of this range.

Be Organized: Once you have a buyer interested in your business, the lengthy process of meetings, discovery, offers, counter offers, due diligence, etc. begins. The buyer will be requesting a lot of information throughout the process. Your broker will be there to help you know the right time to release the information. Having the information on hand will keep the process moving toward a quick close. Items to have ready, clean and organized include three past years and year-to-date financial statements, three past years tax returns, copies of any leases, and internal documents such as organization charts and policy manuals. Not only will having these available keep the process moving along quickly, but it will also put the buyer at ease, seeing you are running a clean and organized operation. A confident and assured buyer is one that keeps moving to closing.

Ultimately, it is important to remember that selling your business is a negotiated transaction, and negotiations require give and take. Before you go to market, identify your top priority in selling your business. Is it a quick sale? Is it to maximize your profit? Is it to assure jobs for your employees? To achieve any of these goals, you will often need to make sacrifices in other areas. If the timeline is your only concern, be prepared to make concessions on price and other terms of the deal. What your business sells for does not equal the amount of money you put in your pocket. As part of our work with businesses owners as they prepare to sell their businesses, we provide business valuations. Knowing the market value of your business (what you can expect the business to sell for on the open market) is a key piece of information that you will need in order to make educated decisions regarding whether to sell, what price to accept, and so on.

On a few unfortunate occasions, I have seen sellers surprised at closing by financial obligations they had overlooked, which ate into their net proceeds. Suddenly, a seven-figure sale price can net only a few hundred thousand to their personal account. Not an ideal scenario. How can that happen? How can you avoid the same fate?

There are three main items to remember as you evaluate a sale price for your business and what it would put in your wallet.

You Will Pay Your Debts: Most small businesses are sold as asset sales. Simply put, the assets of one corporation are sold, free and clear, to another corporation. The emphasis here is on "free and clear," meaning that at closing, before you get any money yourself, any loans and debt you have against the business will be paid in full. Any financed equipment and vehicles will be paid off. Any real estate loans will be satisfied. All balances will be brought current.

In the case of a stock sale, a business owner sells all the stock of their company, and is not responsible for the debt unless agreeing to be as part of the negotiations. Under this scenario however, you must remember that the seller also gives up any claim to receivables.

You Will Pay Your Taxes: One of the two great certainties in life is taxes. Your tax liabilities can vary greatly depending on the allocation of the purchase price (which is agreed to between buyer and seller), your tax bracket, and your personal financial situation. It is of utmost importance that you involve your accounting and tax professional in your sale from the very beginning. They will be able to help you to negotiate an allocation that is favorable to you, and to help you properly anticipate what you will owe Uncle Sam after closing.

You Will Likely Finance a Portion of the Transaction: Almost all sellers begin the selling process by stating they will not finance the purchase. The reality is, they usually must if they want to sell their company. Even a bank financed transaction may require that the sellers keep some skin in the game. SBA loans typically have sellers carry 10 percent of the purchase price, while conventional financing requires more. If a bank is not involved, the seller should expect to finance an even higher percentage of the sale price. This differs from debts and taxes in that eventually you will receive your money, but you need to remember that it is a portion of the sale price you won't be carrying away from the closing table.

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Closing the sale of your business is a big day. You are hopefully rewarded for your life's work, and can set yourself up for a comfortable retirement. Being aware of the factors that determine your net proceeds at closing can be a game changer. Be sure to involve your team of experts, and be prepared for what's ahead.

Chapter 10: Selling Without Regret

"Why do I want to sell?" It's the first question anyone contemplating the sale of his or her business must answer. Price and terms of a transaction will be negotiated and details might fade from your memory over time, but true happiness and peace with your decision to sell hinge on a firm understanding of your own internal motivation.

"Away From" Motivation: These are the motivating factors within your business pushing you to sell. It is what motivates you away from your business. This is how most people instinctively answer the "Why do you want to sell?" question. This form of motivation addresses the things you want to leave behind, in other words, the aspects of your business you are happy walking away from-- the stress, the long hours, having to make payroll, dealing with difficult employees or vendors, etc. However, you must also consider the elements of your business you do enjoy. Giving up one means giving up the other.

For most business owners, this is a pretty easy form of motivation to understand, and is often the initial reason someone considers selling. But to be fully happy with the decision to sell, "away from" motivation can never be the sole motivation factor.

"Toward" Motivation: These are the motivating factors in your personal life pulling you toward a life after business. What are you going to do after you sell your business? What are you moving toward? Many will say they are going to spend more time golfing or fishing. When you have spent the last 35 years of your life working ten-hour days, is that a realistic expectation? Some people might golf that much, but for others, it might be charity work or spending more time with their grandkids. Take the time to consider how you plan to spend your new free time.

It's amazing how many entrepreneurs come back looking to buy a business shortly after they have retired. In 2013, nearly one quarter of all new businesses were started by baby boomers, ages 55-64. If you are deciding to leave your business, it's best to figure out where you are headed, even if that road does lead to another business.

With every year that goes by, I realize that a healthy and happy life is all about balance-- eat your greens and enjoy an occasional dessert, work hard and be home for your family, etc. Selling your business is no different. You must fully grasp both what you

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are leaving behind and what you are moving toward, how they are both pushing and pulling you, and whether that will account for a happy post-business life.

Why do you want to sell? Ultimately this is a question only you can answer.

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