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# 10 Keys to a Successful Exit for Business-Owning Clients

By David M. Kauppi  
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Your business-owning clients have worked long and hard to grow their businesses. Help them exit in a position of strength and get the value they deserve.

Your client started his company 20 years ago "in his garage," worked many 80-hour weeks, bootstrapped his growth, viewed his company with the pride of an entrepreneur, and is now considering his exit.

But the decision to sell is all too often reactive rather than proactive. The primary reasons owners sell their businesses are a serious health issue, owner burnout, the death of a principal, general [industry decline](#), or the loss of a major customer. Don't let your client take such a haphazard approach, which can lead to a much less successful transition.

Oftentimes very capable business people approach the sale of their business with less formality than the sale of a home. Advance planning can ensure that your clients exit their business from a position of strength, not from weakness due to necessity. Talk to your small-business-owner clients now, before a crisis arises, about how they will transition out of their ownership.

Here, we will cover 10 key factors you should discuss with business-owning clients so they maximize this one chance to reap the rewards from their lifetime of work.

## 1. Do not wait too long

Have you ever heard someone lament, "I sold my business too early?" Compare that with the number of times you've heard somebody say, "I should have sold my business two years ago." Unfortunately, waiting too long is probably the single biggest factor in reducing the proceeds from the sale of a privately held business. The erosion in business value typically is most pronounced in that last year before exiting.

Again, owners often wait until the decision to sell is reactive rather than proactive. People who may have spent 20 years running a business and controlling their outcomes often behave differently when exiting from their business. Rather than [planning ahead](#), they are caught off guard by one of the crises mentioned above and are forced to sell in a rush or under unfavorable circumstances.

Thus, encourage clients to think ahead about when to sell while business is still booming, while they are still feeling engaged and enthusiastic about the company and its work. A business should be exited from a position of strength, not from the weakness of necessity. That next big deal can't delay the sale. Instead, an intelligently written sale agreement containing contingent payments can be used to take care of any transaction projected to close.

## 2. Prepare for life after business

We all [create business plans](#), both formally and informally. We all plan for

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vacations. We plan parties. The most important financial event of someone's life, the sale of their business, needs to be planned carefully as well.

Typically, a privately held business represents more than 80% of the owner's net worth. Help your clients think about their plans for enjoying the rewards of their labor. Where do they want to travel? What hobbies have they been meaning to start? What volunteer work have they meant to do? Where do they want to live? What job would they do if money were not in issue? Owners need to mentally establish an identity for themselves outside of their business.

### **3. Spruce up for maximum sale value**

Once the owners are excited about all the fun things they'll do once they exit their business, it's time to focus on what they can do to [maximize the value of their business](#) upon sale. This topic could provide more than enough content for an entire article, but here we will just briefly touch upon a couple of important points.

First, a professional CPA firm should be engaged to do the books. Buyers fear risk. Audited or reviewed financial statements from a reputable accounting firm reduce the perception of risk. The buyer shouldn't be expected to give credit for something that does not appear in the books. If a large percentage of the business comes from a very few customers, the owners should embark immediately on a program to reduce customer concentration.

Buyers fear that when the owner exits, the major customers are at risk of leaving as well. The owners should immediately start delegating management activities and identifying successors internally. If the owners have no one that fits that description and they have enough time, they can seek out, hire, and train an individual who would stay on for the transition and beyond. Buyers want to keep key people that can continue the momentum of the business.

Help your business-owning clients analyze and identify the growth opportunities that are available to the business. What new products could they introduce to their existing customer base? What new markets could utilize their products? What strategic alliances would help grow the business? It's important to capture those opportunities in a document and identify the resources required to pursue the plan. Buyers will have their own plans, but their perception of the value of the business will be increased through a grasp of the growth opportunities.

### **4. Keep your eye on the ball**

A major mistake business owners make in exiting their business is to focus their time and attention on selling the business as opposed to running the business. This occurs in large publicly traded companies with deep management teams as well as in private companies where management is largely in the hands of a single individual. Many large companies that are in the throes of being acquired are guilty of losing focus on day-to-day operations. In case after case, these businesses suffer a significant competitive downturn. If the acquisition does not materialize, their business has suffered significant erosion in value.

There simply is not enough time for owners to wear the many hats of operating their businesses while embarking on a full-time job of selling their businesses. The owner wants the impending sale to be totally confidential until the very last minute. If the owner attempts to sell the business himself, by default he has identified that his business is for sale. Competitors would love to have this information. Bankers get nervous. Employees get nervous. Customers get nervous. Suppliers get nervous. The owner has inadvertently created risk, a potential drop in business, and a corresponding drop in the sale price of his business.

### **5. Be sure to get multiple buyers**

While each case varies, the typical business sale transaction for a privately held business begins with either an unsolicited approach by a competitor or with a decision on the part of the owner to exit.

If a competitor initiates the process, that person typically isn't interested in overpaying for the business. In fact, just the opposite is true; a competitor will be trying to buy the business at a discount. Outside of the owner, no one in a better position than a major competitor to understand the value of the business. The buyer will try to keep the sales process limited to a negotiation of one. That's not in the seller's best interest.

In our mergers and acquisitions practice, an owner often approaches us after receiving an unsolicited offer. By bringing in other offers, what we have found generally is that the unsolicited buyer will not be the ultimate purchaser, but if he is, the final purchase price is, on average, 20% higher than the original offer.

If the owner decides to exit and initiates the process, it usually begins with a communication with a trusted advisor such as yourself, and/or an accountant, lawyer, or banker. Let's say that the owner is considering selling his business and he tells his banker. The well-meaning banker might say, "One of my other customers is also in your industry. Why don't I provide you an introduction?" If the introduction results in a negotiation of one, it is unlikely that the owner will get the highest and best the market has to offer.

## **6. Consider a mergers and acquisitions firm**

Owners improve the odds of maximizing proceeds while reducing the risk of business erosion by hiring a firm that specializes in selling businesses. A large public company would not even consider an M&A transaction without representation from a Merrill Lynch, Goldman Sachs, Solomon Brothers, or other high-profile investment banking firm. Why? With so much at stake, they know they will do better by paying the experts. Companies in the \$3 million to \$50 million range fall below their radar, but there are midmarket M&A firms that can provide similar services and process.

Generally, when a business is sold, it is a once in a lifetime experience for the owner. Those who are buying up companies may have done so many times. Your clients may be excellent business people, they may know their stuff, but when they make this transition it is likely to be their first and probably last business sale. So who has the advantage in this transaction? By helping clients consider engaging a professional M&A firm, you can offer a way from them to balance the M&A experience scales.

## **7. Engage other experienced professionals**

A CPA firm that has the experience to offer advice on important tax and accounting issues can literally result in differences of hundreds of thousands of dollars. What are the tax implications of a stock purchase versus an asset purchase? A lower offer on a stock purchase may be far superior to a higher offer on an asset purchase after the impact of taxes on the realized proceeds. Does your client's current accountant have the qualifications to advise on this issue?

Would the accountant know the best way to allocate the purchase price on an asset sale between hard assets, goodwill, employment agreements, and non-compete agreements? A deal attorney is very different from the attorney you engage for everyday business-law issues. Remember, each element of deal structure that is favorable to the seller for tax or risk purposes is generally correspondingly unfavorable to the buyer, and vice versa. An experienced team for the buyer is under instructions to make an offer with the most favorable tax and reps and warranties consequences for their client. A professional team that can match the buyer-team's level of experience with deal structure, legal, and tax issues is paramount.

## **8. Set reasonable expectations**

The days of [irrational exuberance](#) are over. Strategic buyers, private equity groups, corporate buyers, and other buyers are either very smart or do not last very long as buyers. I hate rules of thumb, but generally there is a range of sale prices for similar businesses with similar growth profiles and similar financial performance. That being

said, there is still a range of selling prices.

So, for example, let's say that the sales price for a business in the XYZ industry is a multiple of between 4 and 5.5 times EBITDA. The objective is to sell the business at the top end of the range under favorable terms. In order to sell the business outside of that range you must have a very compelling competitive advantage, collection of [intellectual property](#), unusual growth prospects, or significant barriers to entry that would justify a premium purchase price.

An M&A firm can be of help here. Think about the process of detailing a car before it's offered for sale; a good M&A advisor will assist in that process for the business. Let's say, for example, that 4 to 5.5 multiple from above was the metric in the industry and had an EBITDA for the last fiscal year of \$2.5 million. The gross transaction proceeds could range from \$10 million to \$13.75 million. A skilled M&A firm with a proven process can move the owner to the top of the industry's range. There's a huge difference between hitting the top of the sales price range versus selling within the bottom range.

## 9. Disclose, disclose, disclose—and do it early

A seemingly insignificant minor negative revealed early in the process is an inconvenience, a hurdle, or a point to negotiate around. That same negative revealed during negotiations—or worse yet, during due diligence—becomes at best a catalyst for reexamining the validity of every piece of data. At worst, it can be a deal breaker. No contract in the world can cover every eventuality if there is not a fundamental meeting of the minds and a trust between the two parties.

Unless owners are lucky enough to get an all-cash offer without any reps and warranties, they are going to be partnered with their buyer for some period in the future. Buyers try to keep the seller on the hook with reps and warranties that last for a few years, employment contracts, or non-competes that last, escrow funds, seller notes, and so on. These all serve a dual role of reducing the risk of future surprises. If future material surprises occur, buyers tend to be punitive in their resolution with the seller. Owners should volunteer to reveal their company's warts early in the process. That will [build trust and credibility](#) and will ensure they get to keep all of the proceeds from the sale.

## 10. Be flexible and open to creative deal structure

Your client should bear in mind that everything is a negotiation. For example, let's say the owners of a business have determined that they want a gross purchase price of \$13 million and all cash at close. Maybe the market does not support both targets. They may be able to get creative in order to reach that purchase price target by agreeing to carry a seller note.

If the sale process produces multiple bids and the best one is \$11.3 million cash at close, they may counter with a seven-year seller balloon note at 8% for \$3 million with \$10 million cash at close. If the buyer is a solid company, that may be a superior outcome than the original target, because the best interest return they can currently get on their investments is 4%. Remind your clients that it is important to be flexible, be creative, and to negotiate the hard parts and preserve the relationship with the buyer.

Your clients may have spent a lifetime of work building a business that could provide them with the income, wealth creation, and legacy that they had planned and hoped for. They prepared and were competitive and tireless in their approach. Now they have one final act of business to conclude. Help them make that their final business success. Help them exit on purpose and do it from a position of strength, receiving the highest and best deal the market has to offer.

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