

## BUSINESS SELLER GUIDE

Deciding to sell your business is an emotional decision. Once you think about selling then it is time to make the move – assuming all decision makers are on board with this decision. Once you decide that you want to sell then make the move. Marv Levy, the NFL Hall Of Fame Coach once said that *“once a player thinks about retiring then he has already retired.”* This statement by the former Buffalo Bills Head Coach and General Manager applies to business owners as well. Once you think about selling then you are already making an emotional move toward selling.

The first area to understand is that books and records are important. A business needs to be able to justify a price through tax returns, equipment values and inventory values. A pure “cash business” with no substantiating data is very difficult to sell. But in these “cash business” situations where the actual cash flow and declared cash flow are different, there are still ways to prove the entire cash flow through a second “book” or receipts.

The second area to understand is that you should keep the business running as is and NEVER tell anyone that you are selling. Any hint or leak that you are selling could be catastrophic to the business and the businesses’ future. Employees and customers are very good at noticing changes that may indicate a business is for sale. This will have a devastating result on the business.

Once the decision has been made to sell, you must prepare various facets of your business before taking the step toward selling.

Here is a general list that you need to prepare...

1. Up to 3 years of tax returns - including P&L statements if available
2. Equipment list & value of equipment at replacement cost
3. Value of inventory at your cost (not retail)
4. Value of real property (if included in the sale)
5. Copy of the lease if business is on leased real property

Here is what you **DO NOT** want to do...

1. Tell anyone that you are going to sell – confidentiality is of utmost importance
2. Change the business models or daily operations
3. Take cash out of the business that will alter subsequent financial statements

Once you have the documentation in place then contact us for a confidential NO OBLIGATION meeting.

## **2. What You Should Be Prepared For**

Be prepared to work hard on selling your business while experiencing various pitfalls that may seriously stress you. There is no perfect business to sell so the work involved in selling your business is intensive and full of legal issues and agreements. Business owners who try to sell his or herself eventually find that they get in too deep into areas where they have no knowledge or experience. At this point this business is almost surely suffering because not only has the confidentiality not been protected but the owner's time has been taken away from running the business and placed on trying to manage their business for sale process.

FYI – business brokers generally work anywhere from 30-40 hours total on the businesses they've sold. And this time has been streamlined and reduced because of their expertise. So it goes without saying that business owners trying to sell on their own will spend more than 30-40 hours – do you really have that time to dedicate in a short period of time?

Next you should be prepared to consider all reasonable offers. The reality is that full offers would be nice but happens less than 5% of the time. If you want your business to sell then you may have to consider taking slightly less than what it was originally valued at. This is also why a detailed market value analysis – covered elsewhere herein – is so beneficial. The ability to fully detail the price is a key to getting offers close to or at listing price.

Buyers are also taught negotiation meaning they may start low and look for you to negotiate back as well. So negotiation expertise is important to deal with buyers. Without it – buyers will drive you crazy.

Next be prepared to frequently meet with buyers. Most buyers are first time buyers and while they have to be qualified they do experience fears of the unknown. Buyers will want to meet with you – frequently more than once – prior to placing an offer. Having the expertise to structure the buyer from presentation to offer is another key ingredient in getting offers.

Last is that you have to be prepared to manage in upwards of 20+ contingencies before and after the offer process. Failure to understand these contingencies will almost surely result in a damaged or failed transaction.

FAILURE TO BE PREPARED COULD RESULT IN A FAILED CLOSING.

If you want a prepared professional representing you then contact us for a confidential NO OBLIGATION meeting.

### **3. The Importance of Confidentiality**

The importance of confidentiality at all times during the sales process is the most important ingredient in the successful sale of an existing business. This IS NOT a real estate transaction where real estate is posted on public MLS services for everyone to find. This is a business with employees, customers, competition and possibly landlords and creditors. By making a business for sale public, all of the above mentioned entities associated with the business for sale will be thrown into a “cause and effect “ flow that will permanently harm the business being sold.

*Ask yourself the following questions relating to confidentiality...*

1. How would your employees react if you told them that you are selling?
2. How would your customers and clients react to you selling?
3. What would your immediate competition do if they knew that you were selling?
4. If you have a landlord – how would they react to you selling while under lease?
5. If you have suppliers etc extending credit – how would they react?

***If you answered the following then confidentiality should be vital to you...***

1. They would leave and/or have a negative attitude worried about job security.
2. They would go elsewhere worried about the quality of the product or service.
3. They would use in their marketing/advertising/sales to sway business to them.
4. They would not be happy and in the worst case could call the lease.
5. If they are extending credit then they may pull credit and go to COD

The extent to which confidentiality is applied goes well beyond what most business owners have knowledge of and access to. There are specific forms and agreements that protect confidentiality. There are entire processes that protect confidentiality.

*If the engine on your vehicle broke down, would you start replacing parts yourself or would you take it to a reputable mechanic? This is no different than a business owner attempting to protect his or her confidentiality. Let an expert protect confidentiality at all times*

-Scott Radin

*North American Alliance of Business Brokers*

**FAILURE TO PROTECT CONFIDENTIALITY WILL RUIN YOUR BUSINESS**

If confidentiality is important to you then contact us for a confidential NO OBLIGATION meeting.

#### **4. The Importance of Qualified Buyers**

Yes confidentiality is vital but so is having qualified buyers to purchase your business. A buyer who is not qualified will only destroy a deal somewhere in the process. A buyer not qualified has no ability to follow through even after an offer has been accepted. This is the single greatest “deal killer” among business owners attempting to sell a business on their own.

Just because a buyer wants to buy a business does not mean that they can buy a business. There are two types of buyers – the qualified buyers and the dream seekers. Unfortunately, with owners selling on their own - the dream seekers do not exit the closet until it’s too late. Qualified buyers are so important.

A buyer should be qualified in a certain way allowing for the real possibility of business financing either through the owner his or herself or by third party lending. A buyer with 100% cash is rare. A buyer wanting 100% financing is dreaming as there is no such thing as 100% financing on a business – anyone who tells you that there is 100% financing is a liar!

There are five factors that determine a buyer’s qualification...

1. Relevant Experience
2. Liquid Capital
3. Source of Liquid Capital
4. Credit Standing

## 5. Motivation

The variables regarding these qualification standards are endless depending on the type of business and the type of buyer. Business owners selling their business on their own underestimate the importance of buyer qualification and are frequently left holding an empty transaction where not only did the sale not take place but the confidentiality was not protected – and the business is now suffering.

Think about it from your own perspective. If you were going to hold a note or mortgage on the business would you do it for anyone or would you want to feel confident that this person would be able to succeed and make payments on time? Third party lending sources feel the same way so qualification is another key component in a successful transaction.

### FAILURE TO QUALIFY BUYERS WILL ALSO RUIN YOUR BUSINESS

If qualified buyers are important to you then contact us for a confidential NO OBLIGATION meeting.

## 5. The Importance of Financing

As mentioned in Section 3 above, a buyer with 100% cash is rare. A buyer wanting 100% financing is dreaming as there is no such thing as 100% financing on a business – anyone who tells you that there is 100% financing is a liar!

So it goes without argument that some sort of financing will be needed to close the deal. There are various options for financing that are covered below with the understanding that buyer qualification is the key ingredient to obtaining financing for the buyer. You want to close right and get paid right? The ability to finance a buyer is the make or break point of getting to closing.

Before jumping into the three main financing categories, let us dispel one myth and that is the misconception that the owner HAS TO hold a note or mortgage on the business to get a deal closed. This is not true and it totally rests with the individual owner's preference. We will advise that selling a business with some amount of owner held financing does make it slightly easier to sell. But we always advise owners to speak with an accountant about the pros and cons to holding the loan on their business.

Three Types of financing...

1. Owner held financing is one option but see the last above paragraph to dispel the myth that an owner has to hold financing. We always advise owners to speak with an accountant about

the pros and cons to holding the loan on their business. There may be some tax benefits to doing it this way.

2. Local bank SBA financing is very difficult for a buyer to secure in the small business for sale environment. It is also the primary reason why there is the misconception that lender financing is difficult. But there is a third and viable option – Acquisition financing.

3. SBA Acquisition financing from third party lending sources is the primary lending source used to fund buyers of small businesses. These sources are specifically in business for small business lending. Most business owners – and business buyers - do not know of these types of lenders nor do they have the contacts to use them successfully.

#### FAILURE TO OBTAIN BUYER FINANCING WILL KILL THE DEAL

If getting a deal closed using reputable financing sources is important to you then contact us for a confidential NO OBLIGATION meeting.

### 6. Placing Market Value on Your Business

One of the truly confusing aspects of a business owner trying to sell on his or her own is that of what value to place on the business. Such thoughts as “it is what I need to retire on” or “it’s what I put into it” are not methods for determining what a business is worth on the market.

Too many business owners also concentrate on gross sales without proper knowledge of the basic operating expenses to profit on their business (**cash flow**). Cash flow is the true profit of the business and the asking price should be a variable on cash flow. Cash Flow - not gross sales - determines the profitability of the business.

#### What is Cash Flow?

Cash flow is profit before taxes. It is what the owner is truly making. Cash Flow is determined by taking the Net Profit or Loss from the tax returns then "adding back" to the Net Profit or Loss any non-essential, non-business related or paper expenses (amortization, depreciation and interest). There are additional "add backs" like one-time expenses or payroll expenses on an employee no longer with the business - just to name a couple.

For example - we have a fictitious business named *Widgets Inc.* In looking at their latest tax return we see that it has a Net Profit (bottom line) = \$68,787.

Automatic “add backs” to profit from the tax returns...

1. \$6,424 Depreciation expense
2. \$3,178 Amortization expense

3. \$1,674 Interest expense

Discretionary "add backs" to profit from the tax returns...

- A. \$12,676 expense for "insurance" was all personal on the owner and wife
- B. \$18,900 expense was a one-time expense for redesigning the interior
- C. \$5,323 expense was for the owner's personal vehicle not made part of the sale not needed to operate the business.
- D. \$4,568 expense was for his yearly dues at the country club - obviously not needed to operate the business.

So in determining the cash flow...

\* Take the Net Profit = \$68,787

\* then "add back" 1-3 above (cumulative \$11,276)

\* then "add back" A-D above (cumulative \$41,467)

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**TOTAL (Cash Flow) = \$121,530**

So while the tax return shows a \$68,787 net profit – the true profit or CASH FLOW was \$121,530. Some businesses will show a loss on their tax returns but a good and positive cash flow.

The actual market value of the business should be determined by using a multiplier of the cash flow + the assets.

If you read terms like EBIT or EBITA and don't understand it. Don't panic. Here is a simplified explanation...

**EBIT** (Earnings Before Interest and Taxes) - Cash Flow Above less Interest

**EBITA** (Earnings Before Interest, Taxes and Amortization) - Cash Flow Above less Interest & Amortization

The EBIT for Widgets Inc above would be **\$119,856** (cash flow less the \$1,674 Interest Expense)

The EBITA for same would be **\$116,678** (cash flow less the \$1,674 Interest Expense & \$3,178 Amortization Expense).

One of the main problems of owners selling their business on their own is that they grossly undervalue their business. This results in far less proceeds from the sale than what they could have gotten by using a professional to assist them.

FYI – back to qualified buyers needing financing (Section 4 above). The comprehensive cash flow analysis to market value is the primary method used by the acquisition lenders to fund the buyers to help a deal gets closed.

There are also Third Party Valuation options to get a detailed value on your business. These valuations can be quite expensive but do provide the most concrete “book” of your business market value.

#### IMPROPER MARKET VALUE METHODS WILL GET YOU LESS MONEY

A good business broker WILL ALWAYS provide you with a detailed analysis of how they priced your business for sale.

If getting the most value for your business is important to you then us for a confidential NO OBLIGATION meeting.

### **7. Who are Business Brokers**

Good business brokers are a trained intermediaries experienced in the confidential sale of businesses for sale to qualified buyers. They usually work for and are compensated by the seller though some brokers do represent the buyer. Some states even allow for dual agency (representation). ASK the business broker who he or she represents.

The benefits to a business owner using a good business broker...

1. Protect Confidentiality at all times
2. Qualified Buyer Processes
3. Financing Buyers through SBA acquisition lenders
4. Placing top market value on the business
5. Continuously targeting and finding new qualified buyers
6. Strategic process to getting offers
7. Strategic process to getting to close

A good business broker represents the seller from buyer qualification till the closing. The business owner can run his or her business while the business broker manages the entire sales process.

*A good business broker is like a sports referee who does a great job – nobody knows he or she is there. The same can be said for a good business broker – they work in the shadows and nobody knows that the business is for sale or sold.*

*-Scott Radin*

*North American Alliance of Business Brokers*

Business brokers are needed to protect the integrity of a business for sale transaction. Confidentiality is the KEY COMPONENT. A good business broker not only finds and brings in qualified buyers but he or she is also an expert at taking the process from offer to close.

**BAD BUSINESS BROKERS CAN DESTROY THE PROCESS**

Don't trust all business brokers – there are three types of brokers – the greedy – the clearinghouse and the one who looks out for your best interest.

If you are looking for a business broker who will represent your best interests then contact us for a confidential NO OBLIGATION meeting.

## **8. Interviewing Business Brokers**

It is very important that you thoroughly interview your business broker before signing an agreement with him or her. FYI – please do not ask for references as part of the interview as a good business broker protects the confidentiality before – during -and after the sale.

### ***10 Recommended Interview questions to business brokers...***

1. How does the business broker protect confidentiality and can they demonstrate the confidentiality processes? *They should have all written materials including the confidentiality documents to leave with you for review*
2. How does the business broker qualify buyers and can they demonstrate it? *They should have all written materials including the confidentiality documents to leave with you for review*
3. What types and how many lending sources does the business broker have that are readily available to finance the buyers? *They should have multiple levels of lending sources and should be able to name a couple of them. They should also have the ability to pre-qualify your business for financing.*

4. Is the business broker fully trained, certified and supported by a reputable source and can they verify it? *This would include a contact person to verify it.*
5. Is the business broker willing to leave you full disclosure materials on their entire process and philosophy? *They should have all written materials including the buyer and seller agreements to leave with you for review*
6. How diversified is the business broker as far as networking affiliations to find qualified buyers for the businesses for sale. *They should be able to list at least a half a dozen affiliations and networking sources – THESE ARE NOT proprietary*
7. How many listing does the business brokers and their agents take. *If it is more than 10-12 listings per broker or agent then how could they possibly give your business for sale the time and resources it needs.*
8. Ask the business broker who they work for - you or the buyer. *This should always be YOU unless dual-agency is a requirement (certain Canadian Provinces only)*
9. Are the business brokers willing to co-broker. *if NOT then you are not dealing with a reputable business broker - you are dealing with GREED.*
10. How does the business broker get paid? *At closing – never before - unless you agreed to a legal retainer to be represented.*

#### AGAIN BAD BUSINESS BROKERS CAN DESTROY THE PROCESS

If you are looking for a business broker who will represent your best interests then contact us for a confidential NO OBLIGATION meeting.

#### ***If a business broker requests or does any of the following – WALK AWAY!***

1. Wants you to sign an agreement on the first meeting- *It can't be done this way. There is no way the broker could accurately place a market value on your business. This is a pressure approach used by unethical brokers and is generally associated with an up front fee or retainer.*
2. Wants a fee to do a market value analysis – *the exception being if you elect to have a Third Party Valuation done – but verify who the Third Party Valuation provider is. Choosing to have a Third Party Valuation done should always be an option NOT a requirement*
3. Requires you to pay for a Third Party Valuation to take the listing – *this should never be required. This is an unethical approach by business brokers to generate an immediate income stream regardless of whether they take an agreement to sell your business.*

4. Discourages you from talking to your attorney or accountant – *this happens too often and is done by business brokers with something to hide – a good broker should encourage you to talk to your attorney and accountant AND be willing to meet with them upon your request.*

5. Requires you to agree to hold a note (seller financing) to take the listing – *this should be your decision and this type of activity is generally associated with brokers who feel the only way to sell a business is with owner financing – not true – they do not have the financing sources to finance buyers.*

The moral of this section is that if you feel uncomfortable or you feel pressured then walk away. Remember that a business broker should work for you NOT vice versa.

AGAIN BAD BUSINESS BROKERS CAN DESTROY THE PROCESS

If you are looking for a business broker who will represent your best interests then contact us for a confidential NO OBLIGATION meeting.

### **9. Fair Payment to a Business Broker**

A good business broker earns their fee through expertise, hard work, networking and sales. They are experts at getting you to close. Reputable business brokers also limit the number of business for sale listings that they take so the fee they earn is well deserved for the time and dedication they put into it.

Each individual business broker has their own fee schedule. Most business brokers charge from 10-15% up to a certain value (contact us for our fee) then decrease this % as the asking price rises.

BEFORE agreeing to this fee – make sure that the broker has outlined for you exactly what they will be doing for you and should include...

1. Determination of a Market Value for Listing
2. The listing
3. Buyer Marketing
4. Qualify Buyers
5. Get Qualified Buyers under Confidentiality
6. Full Disclosure to Qualified Buyers
7. The Tour with the Qualified Buyer the Business Broker and You

8. The Business Financial Review to the Qualified Buyer
9. Due Diligence - Getting Updated Info for Qualified Buyer
10. The Offer
11. Offer Negotiations
12. Accepted Offer
13. Due Diligence Making Sure All Contingencies Are Met
14. Due Diligence Making Sure Financing Is In Place
15. Other Due Diligence Making like Lease or Real Estate
15. The Closing and Dispersal of Funds

In addition, some business brokers charge a retainer though we do not encourage it. Retainers - versus- No Retainers charged by business brokers - what's better? Really there is no right or wrong answer when it comes to retainer or "listing fees". We do not recommend these fees in a normal transaction process though may be used by some brokers in higher value deals. BUT, we also do not necessarily think that retainers are wrong or unethical.

A Retainer or Listing Fee charged by business brokers should only be used and documented for expenses and services rendered. A retainer should not be used as a revenue source for the business brokers. UNFORTUNATELY, most business brokers charging retainer or listing fees use this fee as their primary source of revenue - this is wrong!

### **10. Hiring a Business Broker**

There are many areas of a contract offered by a business broker that you should be aware of. You should always have a written agreement with the business broker - commonly referred to as a Listing Agreement like real estate.

There are terms and stipulations in an agreement that you should understand.

A. The exclusivity of the agreement. An exclusive agreement provides that the business broker under contract is the only business broker authorized to sell your business for the time period allotted. Yes this protects the broker but it also protects you. A business owner under Non-Exclusive agreements opens his or herself up for litigation should two different brokers work the same buyer – assuming both brokers have followed proper disclosure processes. More so, a broker with an exclusive will work harder on it than a broker doing non-exclusive agreements.

B. The length of the agreement. Normal lengths of listing agreements range between 9-12 months. Some agreements can be reduced to 6 months provided there are extenuating circumstances. BEWARE of the business broker offering a short term agreement with a retainer or other up-front fee. This allows them to collect money from you without having to obligate to a long term agreement.

C. The Fee for selling the business. See # 8 above for a break down of fees. The business broker's fee is NOT negotiable under typical listing agreements. BEWARE of the broker who offers to negotiate their fee – this type of broker lacks the confidence and drive to sell your business.

D. Understand and review ALL other contingencies built into the listing agreement. Have the broker explain it thoroughly and – if in doubt – have your attorney look it over.

Hiring a good business broker is the most important thing you can do in selling your business. Like all other businesses, there are good and bad business brokers. You should feel comfortable with who they are and be comfortable with how they have represented themselves. If they refuse FULL DISCLOSURE – that is they do not provide written materials to back up their services then walk away!

**AGAIN BAD BUSINESS BROKERS CAN DESTROY THE PROCESS**

If you are looking for a business broker who will represent your best interests then contact us for a confidential NO OBLIGATION meeting.

### **11. How we can help you...**

We are trained and certified business brokers. A business broker is hired by a business owner to sell his or her business in a confidential manner to qualified buyers. NEVER any upfront fees - we earn it by only getting paid if the business for sale closes. We represent you - the seller - from buyer qualification right through to the closing.

Contact us today