Business Broker Experts

Step by Step Instructions to Sell Your Business

Written by Jim Beno, MBA, Senior Broker

CBI: Certified Business Intermediary

CM&AP: Certified M&A Professional

M&A (Mergers & Acquisitions) Source Member

International Business Brokers Association (IBBA) Member

Midwest Business Brokers and Intermediaries (MBBI) Member

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Step by Step Instructions to Sell Your Business:

The purpose of this report is to give you step by step instructions to follow when selling your business. Think of this report as a secret recipe that is followed by some of the most successful and experienced Business Brokers in the World. If you follow these steps, you will increase your chance of selling your business for top dollar.

Selling a business is very time consuming and statistically will not happen! According to Best Selling author Paul Forsberg in his book, *The 5 Fundamental Elements of Every Successful and Sellable Business*: "You could take any 100 businesses and put them up for sale as they currently operate, and 80 out of 100 will never be sold."

One of the best places you can advertise your business for sale is BizBuySell.com. At any given time, BizBuySell can have 45,000 + businesses for sale. They produce a *Quarterly Insight Report*, below is an excerpt from the Insight Report that tells you about their data:

> "The BizBuySell Insight Report is a nationally-recognized economic indicator that tracks the health of the U.S. small business economy. Each quarter, BizBuySell analyzes sales and listing prices of small businesses across the United States based on approximately 45,000 businesses for sale and those recently sold. The BizBuySell Insight Reports focus on over 70 major U.S. markets and publish local, regional, state and national data for trending and analysis."

BizBuySell can have 45,000 businesses listed for sale at any given time. According to their *Quarterly Insight Reports*, over the last 24 quarters, on average around 2,000 to 2,500 of those businesses listed are sold per quarter, which is about 5% of the businesses listed per quarter. Why is this number low? Mainly, it is difficult to sell a business, increase your odds by following these steps!

Step 1: Determine your cash flow or Seller's Discretionary Earnings (SDE):

Almost all businesses are purchased for the future benefits or cash flows the business will generate. All Buyers will want to review the owner benefits of a business they are considering purchasing. Owner Benefits is also known as Cash Flow or Discretionary Earnings (DE) or Seller's Discretionary Earnings (SDE). To help you calculate your SDE there is a blank worksheet at the end of this report. I recommend you take your tax returns and latest Profit/Loss statement and complete the attached SDE worksheet. You want to use real numbers and make sure you can verify all of your add backs, as a buyer will ask for verification before closing. Your SDE worksheet will be a key tool used to determine a reasonable asking price and also justify your asking price to your buyers, so take your time and complete it accurately.

Step 2: Review a comparison report for similar businesses that sold:

First you need to determine your NAICS (North American Industry Classification System) code or SIC (Standard Industrial Classification) code. To do this go to Google and type in "What is the NAICS code for ______" or go directly to: http://www.census.gov/eos/www/naics and search on your industry. A professional business broker will have access to comparison data if you decide to sell your business with a broker. You may have to pay for comparison data. You can get data on comparative businesses that sold at www.bvresources.com (BIZCOMPS or Pratt's Stats access) or go to www.peercomps.com . You should be able to purchase your Comp report for under $300. If you decide to pay for a comparison report, double check to make sure you have the right NAICS code for your business.

Step 3: Determine your business selling price:

Your comparison data report will give you the number of similar businesses that sold along with the median (average), maximum and minimum multiple of SDE. You can determine a fair asking price based on your SDE and your comp report. There are obviously a lot of other factors that go into determining a reasonable asking price, but this should give you a good idea on what a reasonable asking price is. We offer a separate detailed report that is 10 pages long on how to determine your business selling price. The selling price is adjusted up or down based on the risk of the future cash flows for a new owner. The more risk associated with your business, the lower the selling price will be. Future cash flow risks can be related to how your company is setup or external factors out of your control such as the industry you are in, potential government regulations or the state of the economy.

Step 4: Prepare your confidential marketing booklet to give to buyers:

Your confidential marketing booklet should contain the following information:

- Cover page with the name of your business and an attractive a color photo of the business.
- An introductory page that has your general business information.
- An executive summary, which can be anywhere from 1 to 5 pages long, that should discuss your sales and cash flow for the last few years. The executive summary should highlight business strengths and any selling points of your business. It might also include the benefits of the location, industry information and information on the competition. Any positive statistics about your industry should also be included and referenced. Tell the buyer all the reasons why your business is a great opportunity at your selling price.

- A financial page or Seller's Discretionary Earnings (SDE) worksheet that shows sales, net income, EBITDA and SDE or cash flow for the last three years and the current year.
- Comparison data for businesses that sold with the same NAICS code to justify asking price.
- Term sheet provided from an SBA lender stating the business has been pre-qualified for an SBA loan, if possible. If you can have your business pre-qualified by a preferred SBA lender, this will make your business more attractive to buyers.
- Additional pictures of your business.

Step 5: Create an ad that attracts buyers:

It is crucial that your ad is very generic. You do not want to disclose the name or address of your business in your ads. This information should only be disclosed to buyers who have completed a Non Disclosure Agreement (NDA). No one should be able to determine the name of your business from the ads you run. You do not want your employees, customers or competitors to know your business is for sale! The ad should emphasize your strong points, and do not mention any weak points of your business. The most important part of the ad is the headline. You have only a few words to get the buyer's attention. I recommend writing at least 3 headlines and choose the one you like the best.

Step 6: Advertise your business:

There are hundreds of places you can advertise your business in. If you want to advertise in print media, I would recommend your industry trade publications. Prices will vary on trade publications depending on the size of the readership. Depending on how large your industry is, you will need to be careful what information is included in your trade publication ad. You will get the best global exposure and bang for your buck by advertising your business on the internet. There is no shortage of business-for-sale websites online. Plan on paying about $200 - $600 per ad, depending on what options you choose and how long your ad runs. I recommend running your ad for at least 6 months. If you have an email at your business (Jim@xyzcompany.com) **do NOT use this email address** as it tells everyone looking at your ad the name of your business for sale.

Step 7: Pre-screen your prospective buyers:

After you receive a call or email about your business, request that the potential buyer completes a Non-Disclosure Agreement (NDA) before discussing any confidential information (such as the business name and location). If they do not complete an NDA, do not move forward. If they comply, then send out the confidential marketing booklet you created earlier. Don't be surprised if more than half the inquiries do not take the time to complete your NDA. That is okay, as they are not a serious buyer. This will weed out some of the tire kickers. Again, we strongly recommend all legal documents you use, including your NDA, are reviewed by a local attorney. Laws vary from state to state.

Step 8: Address buyer questions and prepare for buyer meetings:

After a buyer has completed your NDA and you have sent out your marketing booklet, it is time to follow up. Call the buyer to see what questions they have. I encourage you to write down answers to questions you believe will be asked. Having well thought out answers will allow you to have quick and deliberate responses for the buyer. This will help you build trust and credibility with the buyer. This is important, as the buyer continues to request information, they have to trust the validity of the information or they will walk away. This is why earlier in this report I recommended using your tax returns to complete your SDE worksheet. If you provide inaccurate information, it creates doubt in the buyer's mind and they will lose interest fast!

How do you know what questions you will be asked? The best way to prepare for this is to imagine you were considering buying your business. Write down what questions you would ask and prepare answers for those questions. For instance, every buyer will ask why you are selling. If you are under 55 years old, you really need to consider your answer.

Step 9: Request a Letter of Intent (LOI):

The Letter of Intent (LOI) will come from the buyer or the buyer's attorney. The purpose of the LOI is to formally make an offer on your business. It will spell out most of the major terms of the offer such as price, any financing requested, length of time you are expected to stay on for training and other crucial items in the offer. Parts of the LOI are not binding (price, financing, and purchase) and parts are binding (confidentiality of offer, "seller will not discuss offer or negotiate with other buyers").

The presenting of the LOI is the start of the negotiating process. After an LOI is presented you can accept the terms or counter the offer. If you do not already have legal counsel, I highly recommend that you retain local legal counsel before responding to an LOI. My advice on choosing an attorney is to retain an attorney that is experienced in business closings. Attorneys specialize in different types of law. An attorney who is experienced with business sale contracts is who you want negotiating your Asset Purchase Agreement (APA).

Step 10: Work with your CPA and attorney during due diligence:

Once you and the buyer have signed the LOI, you will enter into the due diligence period. Over half of all deals come apart during the due diligence. During the due diligence period, your buyer will request information that is very confidential. It is crucial that all the information you supply is congruent. This is why I recommended using your tax returns to complete your SDE worksheet.

You will be asked to supply several reports / manuals on your business. Items will include financial, employee, customer and supplier reports along with company "trade secret" processes. If any of the information you supply the buyer is inaccurate or contradictory, the buyer may get cold feet and walk from the offer. If this information ends up in your competitors' hands, it could be detrimental to your business. Before you released the name of your business to your buyer, you had them sign a simple Non-Disclosure Agreement. Before you start releasing the confidential information in the due diligence process, your attorney may advise you to have a more detailed Non-Disclosure, Non-Solicit and Non-Compete Agreement signed. **Discuss with your counsel!** The best way to conduct the due diligence is to upload all the requested documents in a secured data room. You don't want to have all of your confidential information in an unsecured site or in paper format where you can't control who is reviewing your confidential information.

If the buyer is comfortable with all the information provided to them during the due diligence, their attorney will put together the Asset Purchase Agreement (APA). Your attorney and the buyer's attorney will go back and forth on the details of the APA and it can take weeks to finalize. The APA is a legal binding contract and includes all the terms and conditions of the purchase. It is enforceable by law and why you want to have an attorney experienced in business sale contracts working on your APA.

You should consult with your CPA **<u>before</u>** the APA is drafted up. I recommend discussing the tax implications of the sale with your CPA before you even negotiate terms of the sale. Before proceeding, I want to preface Jim Beno or Business Broker Experts, Inc. is not providing accounting or tax advice. Every Seller's situation will be different which is why you need to discuss tax implications of your sale with your personal CPA. Below are examples of how the structure of the sale and sale price allocation **could cost you tens of thousands if not hundreds of thousands of dollars in unnecessary taxes:**

What is the structure of your corporation? Are you a C Corp, S Corp, LLC, etc.: Proceeds from the sale of a C Corp will be taxed at the corporate level and when the proceeds are distributed to the owners, this distribution is taxed again. How does the APA allocate the sale proceeds? Some allocations will be taxed as Long-term capital gains (15% - 20% tax rate) and some allocations will be taxed at your normal income tax rates. Your current tax rates, will determine how your CPA recommends you allocate the sale proceeds. For instance, if you are in a 33% tax bracket, you will pay double the taxes on proceeds that are allocated as normal income vs. proceeds allocated as long term capital gains. Besides your current income, your CPA will need to know your current book value of the assets that will be included in the sale in order to determine your tax ramifications. This is another reason you need to discuss the sale with your CPA. Examples of types of allocation would be:

- Goodwill – taxed at long term capital gains rate
- Employment or consulting agreement – taxed at normal income rates

- Non-Compete agreements – taxed at normal income rates or capital gains depending on the structure of the Non-Compete.

Step 11: Close the Deal and get paid:

Once the Asset Purchase Agreement (APA) is agreed upon and the Buyer is satisfied with the entire due diligence documents you provided, you are ready to set up the closing. All the work is done, and it is time to collect your money. You and your attorney will meet with the Buyer and their attorney (many times in the office of one of the attorneys), sign the documents and transfer the funds. If you have a dry closing, your attorney and the Buyer's attorney will just email signed documents back and forth and funds will be wired to your account. Closing requirements will vary from state to state; your attorney will guide you through the process. If you didn't sleep the night before, that is normal. Congratulations! You can now relax!

One of the items we haven't discussed is where the buyer's funds are coming from. If it is a cash deal, you may ask for "Proof of Funds" before you go through the very time consuming due diligence. The buyer can receive a one page letter from their bank verifying that they have the cash available to close the deal presented in their LOI. If you are financing some of the purchase price, you will want to review a credit report on your Buyer.

		2020	2021	2022	2023 YTD	Last 12 Months	Source
1	Sales						
2	Cost of Sales						
3	Operating Expenses						
4	Net Income / Unadjusted Pre-Tax Profit	$ -	$ -	$ -	$ -	$ -	
5	Interest Expense						
6	Depreciation						
7	Amortization						
8	EBITDA *(Lines 4+5+6+7)**	$ -	$ -	$ -	$ -	$ -	
9	Officer / Owner's salary						
10	SBA Adjusted Cash Flow *(Lines 8+9)***	$ -	$ -	$ -	$ -	$ -	

Seller's Discretionary Earnings include the following additional fringe benefits/perks. These line items are company expenses that benefit the owner(s)

11	Payroll taxes related to owner's salary	$ -	$ -	$ -	$ -	$ -	
12	Wages or payments to non-working family						
14	Insurance for owner's health, life, etc.						
15	Auto for owner's personal use						
16	Auto insurance for owner's personal auto						
17	Personal Auto repairs & maintenance						
18	Contributions and donations						
19	Fair market rent adjustment						
20	Retirement Plan Contributions						
21	Non business prof. services (legal / tax)						
22	Other Owner Family Employee Benefits						
23	T&E Meals & entertainment						
24	T&E Travel						
25	Cell Phone expense used personally						
26	One time charges or income						
27	DUES AND SUBSCRIPTIONS						
28	Other Benefits (see instruction page)***						
29							
30							
31							
32							
33							
34	Total Owner Discretionary Add-Backs	$ -	$ -	$ -	$ -	$ -	
35	SBA Adjusted Cash Flow (line 10 above)	$ -	$ -	$ -	$ -	$ -	
36	Total Seller Discretionary Earnings/Cash Flow	$ -	$ -	$ -	$ -	$ -	

Instructions for Completing Worksheet

Your Seller's Discretionary Earnings (SDE), which is shown on line 36, is used to show the financial strength of your business. This number is also used to justify your selling price to buyers. This worksheet recasts your tax returns, which normally report as little income as legally possible, to illustrate the total owner benefits generated by the company. Discretionary Expenses that are added back in lines 11 - 33 are expenses that do not increase the company's sales, but are deducted as a business expense and are a direct benefit to the owner(s) and their families.

* Line 8 - EBITDA: Earnings before Interest, Taxes, Depreciation and Amortization
** Line 10 - SBA Adjusted Cash Flow: Used by the SBA to forecast the company's ability to payback debt

<u>* Other Benefits:</u>**

Use line items 28-33 to add other discretionary expenses - clarify your entry with a short description

<u>Other discretionary expense line items that might be added as Owner's benefits:</u>

- Alarm / Security System Monitoring (Personal property)
- Child Care paid by company or provided by company employees
- Clothing or (dry) cleaning for owner/owner's family
- Excessive rental and/or lease amounts
- Payments related to a vacation house/condo
- Finance Charges
- Household repairs or services paid by the company
- Home Office rent paid to owner by company
- Lawn Maintenance for personal property
- Internet Service for home
- Maid / Housecleaning services
- Memberships (Health, Country or Golf Clubs)
- Non-Business Postage/Shipping
- Personal Credit Cards paid by business
- Product / Services Used (Provided by or paid for by company and consumed by owner/owner's family)