

HOW TO SELL YOUR BUSINESS

A Complete Guide to Maximizing Value





We help business owners
to achieve the **best possible exit**
strategy for their business.

BMS

HOW TO SELL

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The best way to achieve a successful and satisfying exit to your business is to plan the sale in advance. If you are planning to sell your business you should consider the following:

1. PREPARATION

Maximise your business profitability: The profitability of your business is the most important factor in determining its value. By maximising your business' profitability, you will increase the chances of a successful exit.

Work with your accountant to ensure your records clearly and accurately reflect the profit earned by the business: If a buyer is motivated to purchase based on the broader picture, their accountant and other advisers are going to insist on the details before they recommend the purchase. Therefore the first step is to get your books up-to-date. Some businesses prepare financial statements to achieve a favourable tax result. This can have a negative impact on business valuation, if profit in the financial statements is understated below its true earnings. Business Mergers and Sales understands this and has procedures in place to present this in a better format.

Make yourself replaceable: A business is more attractive to prospective buyers if the success of the business is not dependent on the input, technical skill or personal relationships of the owner. As a result a business is best positioned for sale if it "runs itself" without much day-to-day input from the vendor. If you haven't already, look at installing a management team or delegating many of your duties to existing staff. If you remain involved in the daily operations of the business, do so in a general oversight role, which could easily be taken over by anyone with basic business experience or training.

Speak to a qualified business broker: A business broker will be able to provide a valuation of your business, insight into current market conditions and provide other advice on how to position your business to obtain the best result on sale.

2. VALUATION

At **Business Mergers and Sales**, we use the Return on Investment (ROI) method of valuation for the majority of our business valuation. The advantage of using one single method to value a business is that it allows for different for businesses across various industries to be compared to one another on the same basis.

Overview

Adjusted Net Profit x 100 / Return on Investment Percentage (ROI%) = Purchase Price

- Adjusted net profit is equal to the average profit before tax, interest, depreciation and amortisation (*EBITDA*) of a business + add backs over a relevant historical period (average over one to three financial years)
- ROI% reflects the relative risk and growth prospects of a business
- Purchase Price is the total purchase price of a business including assets, such as stock, plant & equipment and goodwill.

Determining EBITDA per financial statements

We use the earnings before interest, tax, depreciation and amortisation (*EBITDA*) as per the financial statements prepared by your accountant. Businesses often have different tax structures and financing structures that do not impact the operations of the business. For this reason, we add back interest and tax expenses as they are not relevant to the assets and earning power of a business. Adding these expenses back also allows us to compare different businesses on a consistent basis.

Calculating adjusted net profit

The starting point for the valuation of a business is the calculation of an adjusted net profit figure for the business over a relevant historical period.

Add Backs

Add backs (sometimes called normalizations or pro-forma adjustments) are used to adjust the reported earnings of a business in order to arrive at a truer picture of its profitability. The type of add backs that are relevant depend on the circumstances unique to each business.

The goal is to adjust the historically reported profit to reflect the economic reality of the business. Typical add backs can include:

- *Donations*
- *Bad debts*
- *Market rent adjustments*
- *Hire purchase and leasing charges*
- *Profit or loss on the sale of fixed assets*
- *One-off expenses*
- *Private expenses (i.e. private motor vehicle expenses put through the business accounts).*

Add backs are an important tool for adjusting financial statements to show the economic reality of the business.

Do we add back the owner's wage?

Investors buying small businesses are often looking to effectively “buy a wage”. For this reason, and to ensure consistency in comparing businesses, we add back the owner's wage for businesses with less than \$500k in adjusted net profit.

In contrast, businesses with an adjusted net profit of over \$500k are presented as being “under management” with the owner's wage expensed at an appropriate market rate.

Determining an ROI%

The ROI% for a business will generally reflect two key factors:

- Riskiness of the business (including industry risk, business specific risk and key-man risk)
- Growth prospects of the business.



A business producing a high net profit but operating in a very competitive market, with little to protect it from having its market share eroded, would attract a higher ROI% reflecting a higher risk and limited growth prospects.

Alternatively, a business with a lower net profit might end up on the market for a similar price because a lower ROI percentage had been applied, reflecting the fact that it had exclusive agencies or proprietary products and thus a high degree of security and growth prospects.

Adjusted Net Profit x 100 / ROI % = Purchase Price

Example 1 (low risk business with strong growth prospects)

\$2,000,000 Profit x 100 / 30% = \$6,666,000 Purchase Price

Example 2 (high risk business with weak growth prospects)

\$2,500,000 Profit x 100 / 50% = \$5,000,000 Purchase Price

Note that in Example 2 the business has higher profit but a lower purchase price due to being in a high risk industry with limited growth prospects.

3. BUSINESS INFORMATION MEMORANDUM

When a business is being marketed, potential buyers often want to seek input and advice from their accountant and other advisers. They might also want to discuss the opportunity with their family and business partners. Once they have considered the basic, primarily financial information which your broker provides, they'll have many more questions about the business such as what will their role be? Are the staff likely to leave or stay? How secure are relationships with key customers and suppliers?

Business Mergers and Sales compile a detailed and comprehensive Business Information Memorandum, covering every aspect of your business including:

- *Business history*
- *Operations including products and/or services*
- *Industry, markets and competitors*
- *Customers and suppliers*
- *Staff details and role of the owner(s)*
- *Premises and lease*
- *Financial performance*
- *Terms of sale.*



The benefits of having a Business Information Memorandum include:

- *It is an effective selling tool in presenting your business in a professional and comprehensive manner to prospective buyers.*
- *Saves time for both sellers and buyers of businesses as most of the questions asked by buyers will be found in the document.*
- *Assists in creating a good impression to advisers of prospective buyers such as accountants and banks. This can assist the buyer in successfully proceeding through 'due diligence' and obtaining finance.*
- *Assists alternate business brokers (who do not have the primary relationship with the vendor) to market the business through their networks as they can understand the business by reading the Business Information Memorandum.*



4. MARKETING

Confidentiality

Most business owners do not want their staff or customers to know the business is for sale.

Marketing a business is a highly specialised field which must meet vendor needs such as confidentiality and compliance with various aspects of the law whilst of the law whilst generating and sustaining interest from potential buyers.

For instance, marketing material designed to be read by the general public will not name the business and usually won't even specify precisely what it does. Yet it must still convey enough information to interest a buyer and elicit a positive response in the form of an inquiry.



Marketing Plan

A marketing plan for every business is developed in consultation with the Vendor.

The marketing plan will generally include:

- *Production of our Business Information Memorandum*
- *Advertising on at least 5 commercial business sales internet sites including **Business Mergers and Sales** web page*
- *Emailing and promoting the business to our database of clients (includes over 4,000 contacts). We maintain a comprehensive database of several thousand potential buyers, providing an instant marketing boost when your business is first listed*
- *Each broker within the firm will promote your business to their network of buyers.*



Networks will generally include:

- *Private buyers looking to own and operate a business*
- *Industry buyers*
- *Investment buyers, including private equity groups and high net worth individuals.*
- *Targeted mail-outs*
- *Advertising in newspapers (including the West Australian) and relevant trade magazines*
- *Targeted approaches to qualified buyers*

Our goal is to execute a campaign which generates as much interest as possible early in the sales process. This creates competition between interested parties, which usually results in a better price and terms through a contested sale.

5. QUALIFYING BUYERS

The objective of our marketing campaign is to generate a large number of enquiries and expressions of interest. Responses to our marketing are then carefully screened. To qualify buyers, we seek to determine the following:

- *Does the prospective buyer have the financial capacity to buy the business?*
- *Does the prospective buyer have the operational capacity to run the business as evidenced by their experience, skill-set and background?*
- *Is the buyer motivated?*

Many business owners who attempt to sell their business themselves report that the process of meeting and qualifying potential buyers is difficult and time-consuming. Distinguishing well-qualified buyers from an array of respondents (including potential competitors) requires experience and background research.

We will maintain confidentiality until a prospective buyer has been appropriately qualified. Then, once a confidentiality agreement has been signed, the Business Information Memorandum provides prospective buyers with a detailed overview of the business operations and qualifies their interest. That way, if you're asked to meet with a prospective buyer, you know they are seriously interested.

6. PRESENTING YOUR BUSINESS

After a buyer has reviewed the Business Information Memorandum and expressed an interest, they will usually have additional questions and want to meet with the vendor. Your broker will co-ordinate this process.

A meeting will be arranged at a suitable time which doesn't interfere with the business' operations and, if necessary, when the staff are not present. Your broker will be there with you when you meet the prospective buyer (and their financial or legal advisers).

7. NEGOTIATING A SALE AND PURCHASE AGREEMENT

It's not just about the price!

When the buyer is satisfied with the information they have been provided, your broker will work with them to draft a Sale and Purchase agreement. The Sale and Purchase agreement will be drafted consistent with the Business Brokers Association General Conditions for business sales. The agreement will include details on the following:

Purchase price: including the assets to be incorporated in the total purchase price and whether this is a share sale or asset sale

Due diligence: giving the buyer a set time frame in which to investigate the business's financial performance and confirm that the information supplied to them is accurate

Finance: including establishing a deadline for finance approval which is to be obtained from the buyer

Restraint of Trade terms: restricting the vendors ability to establish a competing business until a period of time after the sale

Handover provisions: including a familiarization period outlining how long the vendor will need to remain available to the buyer after the sale

Deposit: A deposit of 5 to 10 percent is generally paid by the buyer upon signing the agreement. This is held in Business Mergers and Sales Trust Account

Your **Business Mergers and Sales** broker will liaise between you and the buyer to facilitate an agreement between the parties and ensure that any questions raised by the buyer or their advisers are answered in full and to their complete satisfaction.



8. DUE DILIGENCE AND FINANCE

Due Diligence

The signing of a Sale and Purchase Agreement does not usually constitute the binding sale of your business. The buyer will want to verify the information provided in the Business Information Memorandum and anything they have provided subsequently. If any information has been withheld up to this point due to commercial sensitivity, they will also want access to it.

The due diligence period requested by a buyer varies depending upon the complexity of the business, but is normally about 10 to 20 working days. A buyer can terminate an agreement during the due diligence process, but the depth of information provided in Business Mergers and Sales Business Information Memorandum makes this less likely when compared to other brokers who only provide summary information limited to a few pages.

During this process a buyer will probably want to access information such as:

Financial

- *Financial statements for the last 3 years*
- *Year to date profit and loss from management accounts*
- *Bank statements*
- *BAS statements*
- *Budgets and forecasts*
- *Monthly sales data*
- *Work in progress estimates*
- *Plant and equipment valuations*

Non-Financial

- *Employment agreements and wage details for all staff*
- *Building lease agreement*
- *Any new product development*
- *Customer and supplier lists*
- *Franchise, license, agency and distribution agreements*
- *Insurance policies and claims history*
- *Products and supply lists.*

Finance

A prospective buyer may apply for finance after authorising a Sale and Purchase Agreement. Information additional to the due diligence will often be required to satisfy the bank's requirements.

Your broker will liaise with the buyer's accountant, settlement agent and finance provider to ensure that all of their questions are answered and concerns are addressed. This will help to ensure a smooth process through to settlement.



9. SETTLEMENT AND HANDOVER

After the buyer confirms in writing that all their conditions have been satisfied, the sale becomes unconditional and both parties are obliged to complete the transaction. The solicitors or settlement agents for the vendor and buyer will finalise the details required for settlement, which will be scheduled to take place on a specific date.

This process is considerably simplified (*and thus less expensive for both parties*) thanks to **Business Mergers and Sales** use of specialised Sale and Purchase Agreement.

The deposit held in **Business Mergers and Sales'** Trust Account will be paid to the vendor, less any brokerage fees payable. During the time between the agreement being declared unconditional and the settlement date, the vendor and buyer will need to work together in order to finalise stocktake and the usage of plant and equipment.

Stock take

The Sale and Purchase Agreement will have nominated a stock value to be transferred on settlement.

Stock values are arrived at by calculating the historical cost of purchased stock and, in the case of a manufacturing company, the value of work in progress. A physical stock take will be completed with both parties present a few days prior of the settlement to enable a final stock figure to be agreed upon.

Plant and equipment inspection

The buyer will inspect the plant and equipment detailed in the agreement in order to verify it is in good working order. If any plant or equipment is damaged or faulty, it is the vendor's responsibility to have it repaired or replaced, otherwise its value may be deducted from the total plant value and the purchase price decreased by that amount.

10. POST SETTLEMENT

Handover period

The Business Information Memorandum will usually stipulate a period during which the vendor is prepared to work alongside the buyer after settlement. This will be reflected in the Sale and Purchase Agreement.

However, often the vendor is open to remaining with the business in an advisory or even an active capacity after the sale. The details of this are negotiated and agreed upon prior to settlement and handover. A post settlement checklist will be provided by your settlement agent with input from your business broker. Such items to consider include:

- Advise suppliers, customers and other parties with whom you carry on business
- Immediately advise employees of new ownership
- Organise stock take (if not already undertaken)
- Confirm transfer of power, phone, EFTPOS and other services.



Who Are We?

Business Mergers and Sales is a well established business brokerage firm located in East Perth. Our team has a track record of providing the highest quality business brokerage service in the Perth market.

What sets us apart?

We have a strong track record of providing the highest quality service, documentation, and marketing to all of our clients in regards to business transactions. We are proud to have established new standards of professionalism in the business broking industry in Western Australia.

Our core values as described below:

1. A team environment

We have deliberately cultivated a team environment that encourages a co-operative atmosphere. This means there are numerous brokers actively working on the sale of your business at any given time.

2. 'Client centred' focus

We are a client focused company. It is our responsibility to meet your high expectations as they relate to the sale of your business.

3. Rigorous ethical standards

We are rigorous in our application of the truth to all of our business dealings. We strongly adhere to our fiduciary duty to our clients and the industry standards established by our governing body REBA.

How we benefit you?

We have a long history of practical business experience. We strive to provide the highest quality service possible to all of our clients. Your success is our success. Our focus is on you, the client, and your satisfaction is paramount to us.

For a full confidential discussion regarding your business contact us on:



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