THE EXIT PLANNING REVIEW™

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FORECAST STRATEGIC ADVISORS

Sticking a Toe (or Two) in the Exit Planning Pool

In the previous two issues of this newsletter, we attempted to dismantle the most common objections owners make to undertaking the planning necessary to exit their companies successfully. Those excuses to avoid exit planning are:

1. The business isn't worth enough to meet my financial needs. When it is, that's when I'll think about leaving.
2. I will be required to work years for a new owner.
3. I don't need to plan. When the business is ready a buyer will find me.
4. This business is my life! I can't imagine my life without it!

Assuming we were successful in persuading you that exit planning not only helps your business while you are in it, but is also the best way we've found to leave your company to the successor you choose, on the date you choose and for the amount of cash you want, how do you, as an owner, jump into exit planning?

Let us suggest that one of the best places to jump in is to take some measurements.

First, retain a valuation expert to perform an estimate of value of your company to find out what it is actually worth. (If you plan to sell to a family member, co-owner or employee, retain a certified business appraiser. If instead you foresee a sale to a third party, ask a business broker or investment banker for a "sale price estimate.") The transaction advisor you choose (an investment banker if your company's likely value is at least $5 million, and a business broker for smaller businesses) should be able to give you a range of value for your business in today's M&A marketplace. As we've seen over the past few years, best guesses and educated opinions are nice, but they are weak foundations for exit planning.

Second, sit down with your financial advisor to figure out how much cash you will need to meet your financial needs. Again, tap into the expertise of your financial advisor to help you objectively analyze your future needs and make realistic, risk-sensitive assumptions about investment rates of return.

To illustrate how assumptions, rather than objective measurements, can lead owners astray, let's look at Sam Reed, a hypothetical business owner, who went into a transaction armed only with assumptions.

When Sam Reed started thinking about selling his business, he started paying close attention to what competitors were getting for their companies. He applied his industry's rule of thumb to his company, compared his company to others and figured that his company was worth about $20 million. He calculated that he'd take home about 75 percent of that after taxes. Since he needed $6 million to pay off business debt, he thought he could cash out for $9 million.

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Sam hadn't put a lot of thought into what income he'd need for a comfortable post-exit life, but figured that at his age (50), $9 million, yielding 8 percent per year ($700,000+ annually) would be adequate replacement for the $850,000 salary and distributions he currently took from the business.

With these stars aligned, Sam put his company on the market. Unfortunately, Sam's telescope was out of focus. His idea of business value was unrealistically high, given the flatness of his company's cash flow and the general malaise in the M&A world. The best offer on the table was $14 million of which $11 million was in cash, leaving him with about $2 million net at closing (after taxes and debt payoff) and another $3 million in future payments.

When Sam learned from his financial advisor that the realistic return on the net proceeds ($2-$5 million depending on whether he actually received the $3 million of future payments) was four to five percent, he had no alternative but to quickly back out of the sale process.

Sam made two critical mistakes. He miscalculated the proceeds he'd receive at closing and unrealistically overestimated the rate of future investment return. He would have saved time, effort and money if he had: 1) gotten a sale price estimate which allowed him to realistically estimate how much he would *net* from the sale and 2) forecasted a *realistic, risk-sensitive* rate of investment return (as part of a Financial Needs Analysis). With these two pieces of information in hand, Sam could have made a more informed decision.

Many owners don't have the luxury of time. We suggest that you stick at least your toe in the exit planning pool by taking these two simple measurements. Test your assumptions: you may be surprised at the results.

Call us and we can help you get started on a plan that can make your company more valuable today and help you to achieve the future exit you desire.

Subsequent issues of The Exit Planning Review™ provide balanced and advertising-free information about all aspects of Exit Planning. We have newsletter articles and detailed White Papers related to this and other Exit Planning topics. If you have any questions or want additional Exit Planning information, please contact us.