Valuation, Mergers & Acquisitions

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Considerations in Selling Your Business

Less than 20% of business that go to market actually sell

Emotional and Financial Readiness

Pricing

Where to start.....?

Range of Values

- Owner & Perceived Value → Unrealistic Value
- Sale to an Outside Buyer → Strategic/Synergy Value
- Recapitalization → Investment Value
- Management Buyout → Investment Value (structured)
- Employee Stock Ownership Plans → Fair-Market Value
- Gifting → Fair-Market Value
M&A is a process...some science and some art
Seller’s Goals
- Maximize sales price
- Reduce tax burden
- Accelerate payments from buyers
- Stock sale

Buyer’s Goals
- Minimize the purchase price
- Minimize the unknown liabilities
- Maximize step up basis of assets
- Speed the write off of assets purchased
- Stretching out payment terms
- Obtaining adequate representations and warranties
- Asset Purchase
How Will You Maximize Sales Price?

Follow a Process

Be Proactive

> How do you sell your products & services?

> Make customer want your goods

> They need your goods

> Be proactive in the sales process

Be all in or get all out. There is no halfway.
Motives Not Multiples

- Growth potential
- Customer base
- IP
- Dependable cash flow
- Operational or financial synergies
- Skilled workforce
- Diversification
- ROI

Don’t Price Your Business

- What is someone willing to offer?
- Price is what someone is willing to pay
- The most you will ever receive is......
Maintain Confidentiality

Irreversible Damage can be created by

- Employee perceptions
- Competitor’s leverage
- Customer relationships
- Intellectual property
- Properly time release of information

Target Your Buyer

- Look beyond the obvious
  - Complementary not competitive
  - Foreign and domestic buyers

- Choice is King
  - Invite many to the table
  - Create a bidding war
  - If you don’t like your offer then what?
Sell the Future

- Present a vision of prosperity for the buyer
  - Cross selling products & services
  - Complementary to existing product line
  - What will the buyer’s future look like as a result of acquiring you
  - SHOW THEM!

The M & A Process

External Sales require a process:

- Analyzing viability for sale: 1 month
- Teaser Page, Info. Memorandum: 2 months
- Accepting offers, LOIs: 2 months
- Conducting Due Diligence: 3 months
- Negotiating Final Agreement: 2 months
- Closing the deal: 2 months

Total time: 12 months
The M & A Process

Who has the advantage in the process?

1. Teaser Page
2. Information Memorandum
3. Competitive Bidding
4. Letter of Intent
5. Due Diligence
6. P&S Agreement
7. Closing

Seller

Buyer

So Where Do I Start?

At the Beginning

- It’s not like selling your house
- Maintain CASH FLOW
- Reduce Risk – Implement Value Drivers
- Establish and lock up a good management team
- Clean up your house
  - Legal Issues
  - Financial Statements
  - Contracts
  - Facility
Selling Your Business

Legal Considerations
- Pre closing protection – Confidentiality / NDA
- Letter of Intent
- Due Diligence
- Representations/Warranties
- Purchase and sale agreement
- Non-compete agreement
- Employment agreement

Selling Your Business

Tax Considerations
- Entity Formation
- Deal Structure
  - Assets vs. Stock
  - Cash vs. Financing
- Allocation of Purchase Price
  - Capital gains rates
  - Ordinary tax rates
**Allocation of Purchase Price**

1. IRS Code Section 1060
2. Residual Method - allocate sales price over seven classes
   1. Class I - Cash & general deposits (savings)
   2. Class II - Actively trade personal property (CDs, MS)
   3. Class III - Accounts Receivable
   4. Class IV - Inventory
   5. Class V - Assets not listed in class I, II, III, IV, VI, VII
   6. Class VI - All code section 197 intangibles - (non complete)
   7. Class VII - Goodwill
3. Report on form 8594

**Basis Concept**

**Stock:**
- C Corporation - amount invested at original issue plus any additional paid in capital investments
- S Corporation - amount invested at original issue
  + Additional Capital Contributions
  + Profits
  - Losses
  - Distributions
  +/- Non Separately Stated Items

**Assets:**
- Cost of acquiring assets less tax depreciation recognized since acquisition
Do's

- Come to terms with EMOTIONS
- Have a strategy – ID strategic buyers
- Create a team of advisors to assist
- Reduce lifestyle expenses through business
- Maximize profits and cash flow
<table>
<thead>
<tr>
<th><strong>Do’s</strong></th>
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<tbody>
<tr>
<td>➢ Pre-qualify your buyers</td>
</tr>
<tr>
<td>➢ Invest in your success</td>
</tr>
<tr>
<td>▪ Financials</td>
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<tr>
<td>▪ Valuation</td>
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<tr>
<td>▪ Clean up shop</td>
</tr>
<tr>
<td>➢ Understand timing</td>
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<tr>
<td>▪ Time to close</td>
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<td>▪ Economic timing</td>
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<table>
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<tr>
<th><strong>Don’ts</strong></th>
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<tr>
<td>➢ Take your eye off the ball - maintain operations</td>
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<tr>
<td>➢ Negotiate with one party</td>
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<tr>
<td>➢ Hand over financial information prematurely</td>
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<tr>
<td>▪ NDA</td>
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<tr>
<td>▪ Customer disclosure</td>
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<tr>
<td>▪ Normalization adjustments</td>
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<tr>
<td>➢ Have unrealistic expectations</td>
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Don’ts

- Become overly emotional
  - Timing to close
  - Purchaser’s requests—due diligence
- Close until you understand terms of the deal
  - Taxes
  - Payment terms
  - Continued performance requirements

Questions

Up Next: Interactive Break in the Mezzanine
- How to Integrate an Exercise Routine Into a Packed Life
- Workforce Shortage
- How to Get the Highest Multiple for Your Business Sale: Eight Key Value Drivers for Your Business
- Threats and Opportunities: Operating in the Digital Era
- What Happens When CMs Don’t Manage?