Selling Your Business — Enhancing The Business Value

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When planning for the sale of your business, there are steps that can be taken to enhance or sustain the business value in order to obtain the highest price available. A Chartered Business Valuator ("CBV") can provide expertise to identify the key value drivers within your business and provide insight on initiatives that can strengthen these value drivers.

Sustainable Cash Flows from Operations

A key element in determining business value is the annual sustainable cash flows generated by the business. The historical earnings before interest, taxes, depreciation and amortization would be reviewed to understand the level that is sustainable, and whether there are any discretionary or non-recurring items. An item is considered discretionary if it is reasonable to assume that another business owner would not need to incur the expense to operate the business or if the amounts deducted did not represent fair market value of the services provided. Discretionary expenses may include such items as wages to family members, excess advertising and promotion expenses, rent paid to a non-arm's length party, and excess travel and professional development expenses. Non-recurring expenses may include such items as non-recurring professional fees, repairs and maintenance, and advertising costs.

Having an understanding of how a buyer will view sustainable cash flow well in advance of a sale, and taking steps to minimize discretionary and non-recurring items will provide a clearer image of the business operations to the buyer and reduce the perceived risk of the business. This can result in a higher business value.

Assessment of Your Balance Sheet

In order to achieve the highest value possible for your business, it is recommended you maintain a "clean" balance sheet. This would generally include ensuring that the balance sheet reflects accurate book values for the operating net assets, writing off uncollectible accounts receivable or obsolete inventory, and separate reporting of redundant assets not used in the operations of the business. As a business owner, you should also have an understanding of where fair market value of an asset may exceed the book value reported on the financial statements. This may help a buyer accurately assess the business value.

Supportable Financial Projections

When financial projections are requested by a buyer, management should ensure the estimates and assumptions are supportable and documented, as a buyer will be using these projections to assess the viability of their investment and may result in a higher business value. Regularly updating projections, and comparison of actual results to estimates will help validate that the projections are reasonable and help assess the operating results of the business.

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Managing Working Capital

Working capital, generally the current assets minus the current liabilities of a business, is a common consideration when valuing a business. Buyers will often compare the working capital at the time of close to the amount of working capital they believe is required to operate the day to day operations of the business, and increase or decrease the business purchase price to the extent there is an excess or shortfall of working capital at the time of the sale.

Therefore, an accurate accounting of working capital will prevent unexpected purchase price adjustments and may enhance the business value.

Strong Financial Reporting

A buyer will be relying on the financial information provided by the seller to assess the value of the business. It is important to have accurate, reliable and consistent financial statements. When a buyer has difficulty understanding the financial information, a discount in the purchase price may result, or this may deter the buyer from wanting to complete the transaction at all!

Strength of the Management Team

Development of a strong, experienced management team that can operate the business with limited involvement of the owner enhances the business value, as it reduces the buyer's concern that past financial performance is only because of the prior owner. Instead, it supports that future cash flows are sustainable, which enhances the business value.

Diversify Revenue Sources

A review of the revenue sources of the business may highlight areas of concentration, which can be risky for a potential buyer. Initiatives to diversify products, services and customers may enhance business value.

Review Documentation

Reviewing or creating agreements with key customers, suppliers, and employees will help support the sustainability of revenues and expenses. Reviewing the lease agreement for the business premises will reduce the risk of future unexpected rent increases. Consider negotiating or documenting the opportunity to renew the lease under similar terms. Reviewing existing patents, trademarks, and licensing agreements can help ensure they are properly protected. Buyers will commonly review these types of documents when considering a business purchase, and less value may be placed on an oral agreement than a written one.

For more information on how we can assist you in valuing your business, please contact your **Roth Mosey** advisor.

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