

Value Building and Exit Planning for Business Owners

By Michael F. Coyle, CBI



Michael F. Coyle is the Principal at CenterPoint Business Advisors, Inc. with offices in Franconia, NH and Lexington, MA. Michael is a Certified Business Intermediary (CBI) earned from the International Business Brokers Association and is a member of the New England Business Brokers Association. Michael is a serial entrepreneur and has assisted more than 50 New England-based business owners exit their businesses on their terms.

I'm not usually one for making predictions, but I think I'm on solid ground with these two statements: First, 2008, and perhaps 2009, will not go unmentioned in either history or economics textbooks. Second, being able "to tell your grandkids" is a small consolation as you consider the challenges you and your company face as we endure this storm.

Business owners are getting hit from all fronts. The value of real estate and equity investments are declining due to factors mostly beyond their control. For most business owners the value of their business is the majority of their net worth. The good news here is that the long-term value of your business is most often determined by what YOU do with it rather than external factors. Now, more than ever, is the time for you to set exit goals for your business so that this crucial part of your net worth will deliver to you the life-style you expect in the future. It is never too early for exit planning, but so often you can be too late.

I've given much thought to these challenges lately and I have several ideas about helping you and your company keep on track to achieving your business goals and to eventually making a successful exit from your business. Here are some ideas and strategies to consider:

Get a plan. If you suspect that the current downturn means that you may have to work years beyond your target departure date, or that your business is at risk, objectively analyze areas where you may be vulnerable, set or recalibrate goals, and put new business and personal action plans in place to keep you on target.

Protect your Business Value. Make sure your critical assets are protected from unexpected risks, including loss of trade secrets, customer lists, customer relationships, supply sources, and intellectual property. Establish proper security and implement appropriate employment agreements. Also make sure you have solid contingency plans that protect the value of your assets and minimize tax burdens in the event that you, your partners, or any of your key employees die or become unable to contribute to building company value. Finally, make sure you develop or revisit your Buy-Sell agreements with your partners to be certain that they reflect your current wishes, have valuations that are appropriate, and have proper funding mechanisms.

Grow Value Through Actions of Key Employees. Get key employees on board with properly designed incentive plans and long-term rewards that are in line with YOUR goals and building value of the business. A key value driver of all businesses is a strong and committed management plan.

Consider a Good Offense. Scaling back is usually a business owner's first response to lean times. Consider stepping up your marketing to capture customers who are leaving weakened competitors. While cutting unnecessary cost is always good, this may also be the perfect time to acquire smaller, less adaptable, less capitalized or less well-managed competitors. Certainly this is a buyer's market and there are ways to help minimize your financial exposure while also leveraging strategic value through acquisition.

Prepare for an Exit to A 3rd Party. The M&A market for multi-billion dollar companies has been tenuous, but the market for well-prepared and well-performing companies in the \$5 million to \$150 million range is healthy. While we aren't seeing the multiples we did during the boom part of the cycle, there is financing available for solid transactions in this marketplace. We can't predict when another boom market will occur, but for many of you who are poised to exit your businesses, it will unfortunately not happen in your investment timeframe. Private Equity Groups have hundreds of billions of dollars available to acquire operating companies. These PEGs are looking for profitable companies in the \$5 million to \$150 million range and today are paying good value with reasonable terms. Understand and maximize the key Value Drivers for your business.

If your company is worth less than \$5 million, cash flow is king in realizing value. For companies with good and predictable earnings there are both individual and financial buyers with the ability to finance deals with local banks and business lenders who use SBA 7a and SBA 504 loans. The bottom side of most economic downturns is higher unemployment. Today there are many misplaced, and reasonably capitalized, corporate executives and financial investment professionals seeking the entrepreneurial experience. The features and availability of SBA loans continue to be good and the current economic stimulation package will deliver new equity into these areas. The bottom line is that financing, especially for "smaller" companies may be more available than you thought.

Transferring to Junior If you have planned an ownership transfer to your children, look at the timetable. Assuming your children are nearing an appropriate age, now may be the perfect time to begin that transfer. As you may know, the success of this type of transfer depends less on the value of the company than on the amount of money you receive and the risk you retain. With a reduced business valuation possible due to current business conditions, it should make the transfer to family members much more tax effective.

Transferring to a Key Employee Group (KEG) If transferring your company to your key employees is your preferred exit route, this is an optimal time to begin that transfer. Again, a lower valuation may allow you to bonus your key employees with stock while having minimal effect on business cash flow and with reduced tax considerations for employees. You can bonus that stock so that you retain control until you receive full value for that stock as you simultaneously motivate key employees to stay and build the value of the company.

Get a Team The kinds of business exit planning areas discussed above are complicated and diverse. To be most effective you need a proven process and a team of multi-disciplinary advisors to maximize the outcome. Whether your business value is \$2M or \$150M the same issues exist for the business owner. What may differ is the complexity and depth of the plan. Start with finding an Exit Planning Advisor that can help set a direction and plan, tailor the scope of planning for your needs, and then quarterback the team of specialists that makes it all work (Legal, Tax, Investment, M&A & Business Advisory). You can focus on managing your business and building value.

Don't stand impassively on the sidelines during a time of economic volatility. Unlike the "average" investor, you aren't limited to the single strategy of pulling dwindling assets out of the market. Even if the general economy suffers, your business value need not. Look at your alternatives and get to work. CenterPoint Business Advisors would be pleased to discuss these topics with you or your advisors personally.

Michael F. Coyle, CBI
Principal/Exit Planning Advisor
CenterPoint Business Advisors, Inc.
www.cpointadvisors.com
michael@cpointadvisors.com

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