A WINNING EXIT STRATEGY: THE TOP TEN TIPS

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Exit planning is a broad and complex topic. The right plan depends on the business and the needs and wants of the owner manager. You need to take the time and thought to tailor your exit strategy to your situation. However, no matter who you are or what circumstances you are in, here are ten tips that could make all the difference.

Tip #1 – Do not procrastinate.

You should always run your business with one eye on the exit. After all, you may not control your exit timing. You may not even be around to manage the process.

Here are some example situations:

_ Your death.

_ A critical illness or disability – yours or a loved one's.

_ A sudden shift in market conditions.

_ A sudden loss of key employees, customers or suppliers.

_ An offer you cannot refuse.

Being prepared means you can move quickly and confidently, or someone else can if you are not around or incapacitated.

However, there is an even bigger bonus to starting early. Everything you should do to help you maximize the return on your investment when you sell your business will have immediate positive impact on your business while you continue to own it.

The very things you need to do to get ready to exit your business are the things you should be doing today to get the most out of owning it.

Tip #2 – Make a plan and write it down.

Exiting your business is a process, not an event. It can take years of planning. The better you plan and manage the process, the better it will end.

-You need a written plan to be in control of the process.

-You need a plan to know what success looks like.

-You need a plan to keep track of what you have to do, and how well you and others are accomplishing their goals.

-You need a plan to hold yourself and others accountable for what they need to contribute to your process.

-You need a plan others can follow with or without you, so the process can continue successfully even if you aren't there to direct things.

But most importantly – making a plan will have an immediate, positive impact on you and your business.

Put the plan on paper. Keep it short and to the point. I recommend plans that are ten pages or less. While lots of detail can add weight to a plan, it can also hide the strategic messages or disguise that the strategic thinking is not very good at all.

Share your plan with your professional advisors, loved ones and key confidants. Enlist the support and energy of your closest confidants. It will pay off in the long run. It also will have them ready to carry on if you are unable.

Review your plan regularly, at least once a year. Your plan should be a flexible and living document. It can change as you develop your business, but still be ready to spring into action when the time is right.

Be ready to share your plan with prospective buyers. Make it part of what you have to sell. The best deals are a handing of the torch. You may suggest what still needs to be done with the business and where it should go next. Your buyer will appreciate the help you have to offer. Also, buyers like opportunities that still have upside. Defining that upside will help you attract a buyer at a good price when the time comes to sell.

Tip #3 – Get competent, professional advisors and assemble a good advisory team.

You may only sell or leave a business once or twice in a career. On the other hand, good professional advisors will oversee hundreds of such transitions during their careers, sometimes two or three times a month!

Get people who know what they are doing, have done it many times before, and are cost-effective.

Don't be afraid to change your current lawyers or accountants if you have to. The people that have helped you in the past may not be the best people to help you in the future.

Put together an advisory team to help develop and implement your plan. The team should include:

- Your business accountant.
- Your business lawyer.
- A business valuator.
- A tax professional.
- Your personal financial advisor.
- An insurance professional.
- Your key personal advisors, including your spouse or loved one, key employees, friends and mentors.

There are some limits. The team cannot be so big it's unmanageable. The team should not include people who might react negatively to your moving on, which might include key employees, customers or suppliers. You should have a team that is small, focused, reliable and truly concerned with your best interests above their own.

Tip #4 – Know when to get out (your "triggers").

It is easier to link your succession to a set of circumstances, rather than a fixed date.

Know why you will want to exit your business. There are many potential answers to this question, and your plan should encompass the top three or four.

The first question a buyer or successor should ask you is "Why do you want out?" Having a sensible and well-thought answer is an important part of your exit strategy.

Know what you need to get out of the business before you exit, and why.

Know what things have to be in place before you can move on, and why.

Know how long it could take for those things to fall into place, and what you can do about it.

When you should exit your business is a personal decision. Only you will know for sure. But managing the answers to these questions and having thought out these issues in advance will help you know when the time is right. The answers should also help you develop a plan of what you can and should be doing to get the right set of circumstances in place.

Remember that the existence of the right conditions is more important than a date circled on a calendar or another self-imposed deadline.

Timing will depend on why you are exiting the business.

Timing will depend on what you want and what you need to get out of the business.

Stay flexible – those conditions will not be totally under your control.

In the meantime, as you work on your business, keep in mind that the best businesses to sell are not those that are timing dependant, but which are sustainable, predictable, durable and not based on personality. If possible, develop these characteristics in your business. If you do, timing will become much less important.

Tip #5 – Have a good personal financial plan, and know how your business fits into it.

Owner managers are in it for the money. Maybe they make less money than they could make doing something else, but money is definitely a factor.

For many owner managers, their business is their largest single investment. It can represent a significant chunk of your personal net worth. It may be the single most important key to your financial security.

But you need to know how this asset fits into your personal financial plan, and what you need to get out of it to make your personal financial plan work for you.

It's important to know what you <u>need</u> to get out of your business, and why. You need to consider the minimum you need to get out of your business, especially in financial terms. If you are already set financially, then you are fortunate. If you need money for a new venture, or to sustain you in retirement, then you should be clear on what is necessary so you can build your plan and strategy.

It's also important to know what you want to get out of your business, and why. You need to consider all the things that matter to you when developing your exit strategy, including non-financial issues. You need to shorten and prioritize that list. You may be forced to make compromises, and should have already considered what matters most to you.

Finally, you need to know and appreciate the differences between wants and needs. We all know there is a significant difference, but what does it mean in your case?

It is often a lot easier to get someone what they need than what they want. Having a realistic assessment of your needs can make the whole process a lot smoother.

Tip #6 – Take stock, do a realistic assessment of what it is you have to sell.

The number one impediment to selling a business is almost always the seller's price expectation. Sellers who have trouble selling their businesses usually have an unrealistic assessment of the value of their business to a prospective buyer. If you get a deal on price, the success rate on successfully closing a deal is over ninety percent.

Managing your price and valuation expectation at the outset is essential to a good succession or exit plan.

Ask yourself the following questions and make sure you can answer them. Manage your business around these issues while you are working on your succession plan:

- "How are businesses like mine valued?"
- "What is the present value of my business?"
- "What economic trends impact the value of my business?"
- "What industry trends impact the value of my business?"
- "What is going on in or around my company that is impacting the value of my business?"

This is where your professional advisors come in, especially your business accountant, business lawyer and business valuator. They can guide you through these issues.

Get your business valued by someone who knows what he or she is talking about. Understand how they did it and what factors impact the value of your business from a buyer's perspective.

There are a number of reasons why owner managers over-value their business:

- They don't understand how their businesses are valued generally – especially from a risk/return perspective.
- They don't appreciate that their business is of more value to them than to anyone else since they understand its risks and are confident about being able to manage them.
- They have trouble assessing risk from a buyer's perspective, especially compared to alternate investment strategies such as buying shares in public companies or investment grade real estate.
- They expect buyers to accept returns on investment equivalent to public company price earnings multiples, second mortgages, and other lower risk or more liquid investments.

The key to getting the best price for your business is to manage the buyer's risk perception. The greater the perceived risk, the lower the price and the greater the return on investment the buyer will expect.

Start reducing and managing this risk long before you want to put your business on the market. Do it in a realistic and business-like manner, with lots of input from advisors who may see your business more objectively than you do.

Finally, use this information in conjunction with your needs and wants analysis. Integrate everything you have learned about the value of your business and what you can do to influence it into your personal financial plan. It is important to understand how the value of your business helps or hinders your needs and wants analysis, and what it means to the conditions have to come together for you to exit the business at the right time and in the right way.

Tip #7 – Pick out your successor, plan who you are going to sell to and why.

The most important thing you will need to exit your business is a successor. Start with the end in mind, and manage your plan and business to build a package that will attract the best kind of successor for your wants and needs.

Your choices of potential buyers usually include:

- A partner.
- A competitor.
- A customer.
- A supplier.
- An employee.
- An investor.
- Another owner manager.
- A family member.

Pick your top two or three. Have more than one scenario in mind and mapped out. Know why they would want to buy you out, and what will value most.

Make sure a deal with them is likely to get you what you what you *need* as well as a good shot at what you *want*, both financially and non-financially.

Consider the pros and cons of each kind of buyer, and the kind of deal that would attract them. Different kinds of buyers have different kinds of needs and wants. You need to consider them and see how they match up with your own priorities.

The best deals are win-wins.

Once these choices have been made, prepare your plan and then run and manage your business accordingly.

Tip #8 – Wherever you are today, start working immediately to enhance the value of your business.

Now you have a realistic assessment of what you need to get out of the business and why, what you have to sell, and how buyers are going to look at your business and develop a value and price strategy. But there are still more questions to ask yourself:

- "What could I do that would enhance the value of my business?"
- "What do I need to do that?"
- "What risks do those things represent?"
- "What will it cost me to do those things?"
- "What impact will they have on the value of my business?"
- "What impact will they have on the buyer's perception of risk?"
- "What impact will they have on the profitability of my business between now and the time I sell it?"
- "Are these things finance-able?"
- "What is holding me back from doing them now?"

Depending on the answers to these questions, there may be many things you can do right now which will not only enhance the value of your business when you try to sell it, but may have an immediate impact.

After all, why wait to fix things up if you can reap some immediate rewards?

Again, get help from your advisory team. Business accountants, business lawyers and business valuators all can add value to this assessment.

There are a number of things that impact value and price in the sale of a small business, including:

- ***Profitability*** – sales, margins, overheads – as percentages and in real dollars.
- ***Cash flow*** – to service debt, repay debt, to fund expansion or improvement, to provide reserve, to distribute to owners.
- ***Sustainability*** – profits, cash flow and key relationships.
- ***Predictability*** –consistent, reliable, tied to measurable outside indicators.
- ***Durability*** – robust, adaptable, well positioned.
- ***Believable growth opportunity*** – the more the buyer sees an opportunity for post-closing profit growth, the less they need to use price to manage their risk and the more they will pay.
- ***Finance-ability*** – has the company been managed to leave room for additional third party financing – operating loans, term loans, equipment leases – or potential cost savings and reductions.
- ***VTBs*** – vendor take-back mortgages – are you willing to finance or take back a mortgage for part of the purchase price?
- ***Earnouts*** – are you willing to tie part of the purchase price to post-closing company performance?

_ ***Minimal Personal Goodwill*** - is the company at a stage where anyone can own it and make money?

_ ***Synergy*** – will the buyer reduce competition, or improve margins, or reap cost savings or sales increases?

These are things you can identify and improve while running your business day-to-day. Remember that by this time you will have an idea of who you are thinking of selling to, and what they value the most. You will know how these things tie in to your own needs and wants.

Not only will changes in these areas improve your sale price when you exit the business, they will improve your profits and business during the time you have left.

Consider this analogy: many people fix up their house when they are planning to sell it, and then wonder why they had not taken the trouble to do so during all the years they lived there!

Tip #9 – Attend to the details; get your house in order.

There are some basic things you need to do that will not only impact you when you go to sell but will help you in the meantime:

Plan your ***tax strategy*** and implement it. After all, the only way to compare different offers and deal structures is to compare what they do for you after tax. Get ready for that. A good deal is not about total price, but about how much is left over to put in your pocket

Identify ***redundant assets*** and plan when and how you will get them out of your company. Redundant assets include anything that the buyer won't need to run your business, including excess cash, investments, car leases, cottages, airplanes, etc. There may be hidden value in your company that you could get out now.

Understand how ***EBITDA*** – earnings before interest, taxes, depreciation and amortization – impacts valuation and price negotiations. Set up your accounting and reporting systems to track it. Once you know what factors go into evaluating your business from a buyer's perspective, make sure you have the management reporting systems in place to track them. They will help you know if you are doing the right things to grow the value of your business, and will also create a track record you can share with a potential buyer.

Get the right ***relationships*** with the right people and maintain them. This includes customers, suppliers, employees, and lenders. You want relationships of value that you can pass on to your buyer. Where necessary and possible, you want those relationships documented. Things like non-competition covenants and financing commitments can be very important to a buyer. The more "good things" a buyer discovers during due diligence the greater the prospect of closing a really good deal.

Get your company properly ***financed***, with some excess borrowing capacity on the table. Look at how your business is financed from a buyer's perspective. Steer the business in a direction that is easily financed for its operations, but also leaves some room for the buyer to lever the business to buy you out. The more the buyer can finance from third parties or his or her own resources the better the deal will be for you. The more the buyer needs you to be a lender in order to give you the price you want, the more difficult the deal can become and the more at risk you will be after closing.

Have a “clean” situation on all ***legal and government matters***, including any kind of taxes or government reports or remittances, and especially major contracts such as supply contracts, customer contracts, leases, insurance, financing and employment agreements. Make sure that you are complying with all your legal obligations and you can prove it during due diligence.

Get some ***third party studies*** done if they will help you manage all of this – environmental, structural, marketing, equipment appraisals, business valuations. If you do some of the legwork that a buyer will do, you will have more insight into how a buyer thinks, can take corrective action before a buyer is on the scene, and will have a persuasive story when the time comes to go to market.

Again, the lesson is preparation. As an owner manager you may have gotten used to flying by the seat of your pants. That kind of approach is not a great way to go about selling your business or implementing a succession plan, especially when you consider the risk that you may not even being around to manage the process at all!

Tip #10 – Prepare yourself, prepare your successor.

Finally, remember to prepare yourself on a personal level.

Be sure that that you will recognize when the circumstances are right and act accordingly.

Be sure you can let go.

Be sure you have something else to do that you are genuinely looking forward to.

The number one impediment to making and implementing a good exit strategy is an owner who hangs on too long. Don’t fall into that category.

If at all possible, prepare your successor. Make sure they will have the support of your stakeholders. Make sure they will appreciate the value of the business. Make sure they can finance the purchase for a price and terms you can live with.

And most of all, make sure you and your successor will be enthusiastic partners in helping each other’s dreams come true.