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**8:30 – 9:30**
**Uncovering the mystery of business valuation**

- Boomers still own the majority of businesses in the U.S.
- But they are looking to slow down, travel, spend time with grandchildren, or their health is declining, or they're just ready to let someone else deal with the day-to-day challenges
- Business valuation is an important step in succession or exit planning, and necessary when dealing with buy-sell agreements, some bank transactions, etc.

## Value

- What is the value of something?
- It depends on what we mean by value.
- There are different types of value.

## Economic Value

- Important concept because business valuation involves economic value
- If you were dying of thirst, how much would you pay for a bottle of water?
- $2? $5? $10? $20?
- Economic Value is the value a person places on something based on the benefit they will obtain from it
- Economic Value is subjective; unique to the buyer; and from their perspective
- Economic Value is the reason why one buyer is willing to pay more than another buyer

- Economic Value takes into account intangible factors such as good will, the intentions of the buyer, and synergies that make the acquisition so valuable to a buyer
- The problem is that we usually don't know who the buyer is when valuing a business
- Because of this, Economic Value is difficult to measure
- In fact, it's really not measured, it's negotiated
- BUT we can value what we can measure
- That gets us part way there
- Negotiation gets us the rest of the way
- There are many different ways to obtain a business valuation
- My accounting firm offers business valuations starting at $15,000, performed by an experienced and certified valuation expert

- That's one option but there are others
- And you can get a reliable valuation without spending that kind of money.
- We're going to look at some common methods today

**Market Capitalization**

- Share price x number of shares outstanding
- Example: ABC Corp's stock price as of yesterday was $100. There are 1 million shares outstanding. The market cap value is $100 million.
- Market cap value fluctuates daily.
- Great for publicly-traded businesses.

**Times Revenue**

- Annual revenue x multiplier.
- Multiplier based on a number of factors, including the industry and economic environment.
- Multiplier may be greater or less than 1.0, depending on the industry and specifics.
- Great for start-ups with no profits yet.
- Amazon was founded in 1998 – lost $241M in 2014 – small profit in 2015 and then began to grow its bottom line – made $30B last year.

**Earnings Multiplier**
- Annual profit x multiplier.
- Profit is EBITDA (Earnings Before Interest, Taxes, Depreciation, and Amortization).
- Multiplier is based on a number of factors, including the industry and economic environment.
- Preferred method for our industry.

**Discounted Cash Flow**
- Based on projections of future cash flows.
- Uses discounted cash flow financial modeling to determine present value, taking into account growth and inflation.
- Great for companies with high growth potential.

**Fair Market Value**
- Important legal concept.
- FMV = the price that a willing buyer and willing seller would agree on if neither were under any compulsion to buy or sell and both had reasonable knowledge of the facts.
- Sounds like EV, doesn't it…

**Book Value**
- The value of an asset as shown on a company's balance sheet.
- Buy asset for $10,000
- Depreciation of $5,000
- Book Value is $5,000
- Not used for valuation but important consideration for taxation purposes

**Depreciation**
- How many years can you depreciate an asset? Depends on the type of asset.
- Land? Zero – not subject to exhaustion or wear & tear
- Residential rental property? 27.5 years
- Non-residential real property? 39 years
- Equipment/machinery? Up to 20 years

- What convention is used?
- Buildings (res and non-res)? Mid-month
- Equipment/machinery? Half-year
- What happens when you sell equipment/machinery and the sale results in a gain but the gain was caused by depreciation? Recapture – gain is treated as ordinary income

**Liquidation Value**

- Net cash received if assets are sold and liabilities are paid off immediately.
- Usually used when something bad has happened.

**Simple Valuation Method – Earnings Multiplier**

Step 1

- ➢ Determine EBITDA (Earnings Before Interest, Taxes, Depreciation, and Amortization).
- ➢ Consider earnings trend over 3-5 years and extraordinary items.

Step 2

- ➢ Determine the owner's benefit.
- ➢ Consider any expense paid by the business for the benefit of the owner and that will not be present after the sale.

Step 3

- ➢ Add EBITDA and owner's benefit.
- ➢ This is the anticipated profit after the sale.

Step 4

- ➢ Determine the applicable Earnings Multiplier.
- ➢ Consider industry-specific multipliers, premiums, and discounts.

| Enterprise Value | Up to $500,000 | $500,000 to $1,000,000 | $1,000,000 to $2,000,000 | $2,000,000 to $5,000,000 | $5,000,000 to $50,000,000 |
|---|---|---|---|---|---|
| Multiplier Range | 2.0 to 2.5 | 2.5 to 3.0 | 3.0 to 4.0 | 4.0 to 5.0 | 5.0 to 6.0 |

Step 5

- Multiply Adjusted Earnings (EBITDA + Owner's Benefit) by Earnings Multiplier.

Example:

- EBITDA = $250,000
- Owner's Benefit = $150,000
- EBITDA + OB = $400,000
- Earnings Multiplier = 3.0
- $400,000 x 3.0 = $1,200,000
- What about economic value?
- How good of a negotiator are you?

**Valuation Drivers**

**1**

### Financial Performance

Your history of producing revenue and profit combined with the professionalism of your record keeping.

- How "clean" your books are
- How defensible your financial reporting is
- Prepared by CPA?
- Audited by CPA?

**2**

### Growth Potential

Your likelihood to grow your business in the future and at what rate.

- History of growth over number of years
- Tangible evidence that shows future growth

**3**

## Switzerland Structure

How dependent your business is on any one employee, customer or supplier.

- Key employees (not owner)
- Large customer
- Vendor with too much control

**4**

## Valuation Teeter Totter

Whether your business is a cash suck or a cash spigot.

- Working capital is sufficient
- Not putting money into company

**5**

## Recurring Revenue

The proportion and quality of automatic, annuity-based revenue you collect each month.

- Subscription revenue
- Generac example – told me about maintenance but didn't offer it (fail)
- HVAC people – come out four times a year – no idea what they charge (and don't care)

**6**

## Monopoly Control

How well differentiated your business is from competitors in your industry.

- What's unique about your company?
- Your people? Culture? Values?
- Do you actually keep your word?

- Do you answer your phone?

**7**

## Customer Satisfaction

The likelihood that your customers will re-purchase and also refer you.

- Net Promoter Score (NPS)
- The Ultimate Question: on a scale from 1-10, with 10 being the highest,
- how likely are you to refer us to a friend or relative?
- 9-10 Promoter
- 6-8 Passive
- 1-5 Detractor
- Used by major corporations to measure customer satisfaction
- Some buyers require a high NPS (ignorance is not bliss)

**8**

## Hub & Spoke

How your business would perform if you were unexpectedly unable to work for a period of three months.

- Steps to take that promote distributed decision-making and accountability
  - Develop a strong Leadership Team
  - Implement EOS

**Value Builder System**

As an attendee of this session, we're providing a complimentary Value Builder assessment – a valuation of your business using an online platform – Value Builder System – gives you a very nice report with a complete business valuation and scoring on each of the eight value drivers I just mentioned.

According to the Exit Planning Institute
Over half of all businesses today are owned by Baby Boomers, but…
Fewer than 30% will make it to the next generation or be sold.
Over 70% will be liquidated.

According to the Family-Owned Business Institute,
80% of business owners intend for the succeeding generation to take over, but…
Fewer than 20% have begun planning for succession.

Most adults in the U.S. don't have a will, even though they are free.
In Michigan, we have what's called a Statutory Will.

**9:45 – 10:45**
**Are you ready to exit your business?**

**When is the best time to exit your business?**

- When your business is ready (at its peak)?
- When the market is ready (lots of buyers)?
- When you are ready?
- Ideally, when all three of these occur simultaneously!

**Is Your Business Ready?**

- If you were in my last session, you learned about the 8 drivers of biz valuation…
- Your business is not ready until these 8 drivers score high enough
- Or you're leaving money on the table

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**Is the Market Ready?**

- Currently, yes.
- Will this seller's market last? Probably.
- What's fueling it?

- Strategic roll-ups
- Private equity (family offices, private wealth managers)

**Are YOU Ready?**

- Topic of this session

**Old Saying: "Failing to Plan is Planning to Fail"**

- Has some truth to it, doesn't it…
- Why do people tend to avoid succession planning?
- Common excuses include:
  - I'm too young
  - I'm too busy
  - I have no idea where to start
  - It will be too expensive
  - I don't want to face my own mortality
  - I'll get to it after (____________)

**Who Is Succession Planning For?**

- Is it for YOU?
- Or is it for those you will leave behind?

**What will your legacy be?**

- From whose perspective?
- Will you leave behind a legacy of taking care of others?
- Of being a provider?
- And filled with fond memories?
- Or will you leave behind a mess?
- A clean up job for others to deal with?

**Who are you leaving behind?**

- Spouse, kids, grandkids, great grandkids
- Business partners and their families
- Employees and their families
- Customers and their families
- Vendors and their families

- Extended family members
- Community organizations that you have supported over the years
- ALL of these people will have something to say about your legacy

**Gramps**

- Born in 1902 – grew up poor in a huge family (common in those days)
- Moved to the "big city" of Grand Rapids in the 1930's
- Found success in sales
- Started our family business in 1940
- Grew the business, acquired real estate, became a wealthy man
- Provided for multiple generations
- BUT Failed to set up his business for succession
- When I went to business school, there was no plan for continuing the business into the third generation (my generation)
- Gramps was a great man but he wasn't much of a visionary
- That's his legacy from my perspective

**Protecting your Legacy**

- Begins with your succession plan
- Your **strategic plan** for building your business so that it is transferable when you're ready.
- The plan should include:
  - Your future,
  - Your family, and
  - The business itself.

**Strategic Planning**

- EOS is one of the best systems (explain it)
- Value Builder adds valuation goals (makes EOS come alive)
- Why not "exit" now before you need to?
  - Get your LT in place and disappear
  - Let others step up
  - Allow mistakes (that's how people learn)

**Preparing to Exit – 3 Steps**

**Step 1**

- Plan your future (post-succession)
  - What do you want to do?
  - What are you called to do?
  - What are you passionate about?
  - Where can you make an impact?
  - What is most important to you (joy, peace, satisfaction)?
  - Common for business owners to regret selling b/c they weren't ready
  - Didn't put in the work before to clarify their future

**Step 2**

- Get essential documents in place:
  - Wills
  - Financial & Medical powers of attorney
  - Trusts
  - Buy-sell agreements
  - Life insurance policies & beneficiary designations
  - TOD/POD designations / Ladybird deeds

**Step 3**

- Assess your readiness to exit
  - Complimentary PREScore assessment and personalized report
  - Just need your contact information on clipboard

**Resources – Phil's Companies:**

- tamariskadvisors.com
- growthebench.com
- snowfightersintitute.com

**Other Resources**

- eosworldwide.com
- Value Builder Score – you will receive an invitation
- Personal Readiness to Exit Score (PREScore) – you will receive an invitation