THE EXIT PLANNER

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WHAT'S INSIDE

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GIRDING YOUR LOINS AND MORE

In this issue of *The Exit Planner*, Ned Minor, an attorney with over twenty years of experience representing business owners involved in the sale or purchase of a business, describes some of the "intangible" concerns owners wrestle with **before** they begin the Exit Planning process.

Business owners typically don't decide one day to impulsively leave their businesses any more than a first time skier decides to strap on a pair of skis and plunge down a steep slope. In both situations, there is a large dose of prudence, self-doubt and reflection: "Is this something I really want to do? Now? After all, I can always start tomorrow."

There's an old English term that describes the process well: girding one's loins. It means to prepare for action, such as strapping on a sword; to muster up one's resources. Girding your loins is critical before a first ski run. Girding one's loins is also necessary for business owners **before** beginning the process of leaving their businesses. This article describes, from the perspective of a transaction attorney who has guided hundreds of business owners through the transaction process, how business owners mentally and emotionally prepare themselves. Ned Minor has watched some owners take the plunge and some owners hold back—sometimes disastrously—until conditions change and the prospects of a successful exit (like the snow conditions for a successful ski run) have melted away.

Ned Minor raises the three most common issues business owners tackle as they prepare to take the plunge. First, "**What will I do after I have sold my business?**" While this seems to put the cart before the horse, the inability to comfortably resolve the issues underlying this question prevents too many owners from beginning the Exit Planning process until it is too late.

Second, owners wrestle with timing: "**When should I sell my business?**" This, too, is a deceptively simple question. Yet, as Ned relates his experience with owners, while timing may not be everything, it can certainly mean millions (dollars, that is). Ned's observations on this issue provide a perspective that is unfamiliar unless you are in the transaction business.

The final question, "**Why should I sell my business?**" redirects the business owner's attention to the reasons he or she started a business in the first place. While lawyers, CPAs, Investment Advisors and other transaction advisors are skilled in their fields, they can't answer this question for you. Only the owner can answer this question and Ned shares his experience watching countless owners answer it for themselves.

It is the goal of *The Exit Planner* to help business owners successfully exit their businesses. Exiting your business will never be easy. With proper thought, planning and action, however, it can be successful. Without answering the questions posed in this issue of *The Exit Planner*, your Exit Plan may never begin.

THE TOP THREE QUESTIONS BUSINESS OWNERS ASK BEFORE SELLING THEIR BUSINESSES

By Ned A. Minor

In the course of my practice, I have observed that each business owner brings his or her own set of concerns, circumstances and goals to the transaction process. Despite the wide variety in the types of businesses they own, there are ingredients common to all successful business owners as they contemplate leaving their businesses. Please note that I use the word "sale" and "selling" for brevity's sake only. "Selling" is meant to include the transition of a business between owners or from an owner to key employees or from an owner to his children. This discussion is relevant to any owner who is preparing to transition out of a business.

In this article, I will discuss the three questions I am most frequently asked by business owners who are contemplating selling their businesses. These are the three questions that indicate to me that the owner is mentally preparing to embark on the Exit Planning process.

QUESTION 1: WHAT WILL I DO AFTER I HAVE SOLD MY BUSINESS?

Although this may seem an unusual place to begin, it is the question I am most frequently asked when a business owner first seriously starts thinking about selling.

Most business owners are quite naturally wary of the prospect of selling their businesses. For years, building and nurturing their companies have been the focal points of their day-to-day existence. For many business owners, everything, including friends, family, community and personal desire have taken a back seat to their intense drives to survive and to succeed. Their self-image is defined as "The Owner." Rarely is any decision made without relating its consequences to the business. Quite understandably, it is difficult to foresee a personal identity separate and apart form that of "business owner."

If this sounds all too familiar, don't worry: All of these concerns will resolve themselves if the sale of your business generates personal financial independence. You must, however, accept the fact that after you have completed the sale, you will still be the same person, motivated by the same goals.

The same except that you will have exchanged your illiquid business for financial freedom. Instead of focusing on what it takes to survive as a business owner, you will focus on what it takes to fulfill yourself as a person. Each day your activities will be based upon priorities that you have established instead of responses to business demands thrust upon you by others.

Former business owners rarely spend the rest of their lives just playing golf. Most re-channel their energy into ventures that create additional wealth (with less risk) financially and personally.

I firmly believe that if you are smart enough to start a business, smart enough to make it successful, and most importantly, smart enough to figure out the right time to sell your business, you are smart enough to figure out what to do for the rest of your life with your newly obtained financial independence in order to be happy and fulfilled.

I can't tell you what it will take for you to be happy over a long period of time. I can, however, share my observations as to how many of my clients have dealt with their "PSSAS" (Post-Sale Separation Anxiety Syndrome).

After you have sold your company I suggest that you plan on doing absolutely nothing. This is not as easy as it sounds. If you are like most hard-charging entrepreneurs, you will need to learn to relax. While running your business, you were extremely focused, disciplined and creative. You, of all people, know that it takes a tremendous amount of sustained energy to achieve success.

On the day you "close" on the sale of your business you will have several conflicting emotions. You may feel simultaneously elated, relieved, melancholy and nostalgic. The closing itself is anticlimactic. You will feel a sense of letdown and apprehension, e.g. "What do I do now?" It will simply take time to absorb the fact that you are off that disciplined, high-speed treadmill that was your former business life.

Remember, however, that even while you were on that treadmill, you had a personal life. You traveled (albeit occasionally), golfed, skied, read, spent time with your kids, took photographs or volunteered with your favorite charities. Something helped you to decompress from the stress of business. Once you've closed the sale you will have the opportunity to enhance and to cultivate the activities that you enjoy.

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It is imperative that you learn to relax. Having fun is the best way I know of relaxing. Take a trip with your favorite person to that special place you have often dreamed of. Immerse yourself in golf and achieve the handicap that will cause all of your golfing buddies to select you for their partner. Buy those expensive toys that will enable that "kid" inside you to reemerge. The list of fun things to do is limited only by your imagination (or lack thereof). Go ahead, indulge. You've earned it. Don't feel guilty about not being productive. This is your time to decompress.

Another concern common to business owners is that by selling their businesses they will lose their "platforms" in the community or in their trade associations. They are worried that once separated from their businesses, their status as highly respected civic leaders and leaders in their industries will be in jeopardy.

This should not be the case if you stay active and involved in the same organizations you've always belonged to. Just remember, people will think more highly of you now than ever before. They will refer to you with a certain amount of awe, respect and yes, envy. "Did you hear that John made a killing when he sold his company?" You've known people who have successfully sold their businesses. What were your thoughts when you heard the news?

Colleagues and competitors are envious because you were shrewd enough to develop and execute an exit strategy. This attitude and respect is nourished by their speculation that you have sold the company for far more than you actually did. Savor this respect. Again, you've earned it.

Consider establishing your own private foundation. Nothing maintains high profile and visibility in the community more effectively than going into the business of giving money to worthwhile causes. You will have all of the influence and attention you ever wanted—and more.

Most of my clients simply cannot repress their entrepreneurial instincts. When you were running your own business you had to live by the golden rule: "The person with the gold makes the rules." Now that you have sold your business and are financially independent, you are the person with the gold and now you make the rules. If word gets out that you are looking to invest in business opportunities, you will have a new full-time job sorting through and selecting those opportunities that meet your investment criteria. If your terms and conditions for investment aren't met, you politely decline and start reviewing the next available opportunity. There is no such thing as the last good deal.

When you find the right investment opportunity and it is on your terms, then you choose how active or passive you want to be in the management. You will probably want a seat on the Board of Directors, thus enabling you to remain active in the business on a regular basis. In addition to keeping you in touch with your investment, you will be able to tell all of your golfing buddies that you are "dabbling" in this and that company.

I guarantee you that after the initial period of adjustment, you will discover so many fun, interesting and challenging activities that you will wonder how you ever had enough time to run your business. If you remain unconvinced, I have one last assurance: in all of the transactions I have ever completed, I have never once had a client return and complain, "Gee, Ned, I wish I had never sold my business."

QUESTION 2: WHEN SHOULD I SELL MY BUSINESS?

There are two sets of reasons that dictate the "timing" for selling your business. One is personal and the other financial. The personal reasons are too numerous to describe in detail here and you are already well acquainted with the thoughts that go through your head (at least ten times daily) with regard to selling your company.

The most common personal reasons include: burn out, boredom, diminished challenge, the complexity of the business exceeds the owner's abilities, and less tolerance for risk.

From an economic standpoint, the best time to sell your business is the point at which a sale yields financial independence. I define "financial independence" as having enough principal invested to generate an annual cash flow that supports the type of life you have always wanted to live—without ever having to draw upon the principal. For example, if your goal is to have an annual income stream of $300,000 before taxes, then you must sell your business for approximately $6 million. Generally speaking, if you sell your company for $6 million, you will net, after taxes and transaction costs, approximately $3 million. This $3 million, invested at a conservative rate of return of 10 percent, will yield an annual cash flow of $300,000.

If you are convinced, after consulting your professional advisors, that no matter what management decisions you make, your company will never sell at a price that will generate financial independence, then you must ask yourself, "Am I in business just to pay myself a salary or to generate personal wealth?" If your goal is personal wealth, you should consider two courses of action.

First, you can grow by acquisition, e.g., buying competitors or making strategic acquisitions. Second, you should consider selling your company at its maximum price and reinvesting the proceeds in another company that will ultimately generate financial independence. I have represented numerous entrepreneurs who have followed these paths. They have bought and sold several companies, each one bigger than the one before.

To obtain the maximum sale price, you should sell at a time when you can demonstrate that revenues and profits have increased consistently over a period of time. Don't be lured into thinking that the best time to sell is at the peak of this upward trend. Buyers won't pay top dollar in this situation because they have no room to grow. They have no "upside" potential. Similarly, you want to avoid selling when revenues and profits have been consistently flat. You definitely do not want to sell if they have been steadily declining.

A couple of years ago, I referred one of my successful clients to a top investment banking firm to perform a valuation on his business. The investment banker felt confident that the business could be sold for approximately $25 million. With that piece of information, my client and I adjourned to a nearby coffee shop to discuss what he should do. He confessed that selling his company for $25 million would give him a lifestyle far better than anything he had ever dreamed of. He would certainly achieve "financial independence."

Being a typical entrepreneur, however, my client speculated that if he kept the business for another three to five years he would ultimately sell it for twice that amount, i.e., $50 million. I reminded him that he had just said $25 million would give him financial independence. I observed that if he chose to roll the dice, he did so not for financial reasons but rather for ego, greed and the excitement of being in the hunt. I warned him that there was no guarantee that in three years he would be able to sell the company for a higher price or that he would even be able to sell it for the $25 million quoted by the investment banker.

Within eighteen months of that meeting my client's industry experienced significant negative change. My client was now more than ready to sell his business. When he had the same investment banker do a second valuation, he learned he would be lucky to sell the company for $10 million. Needless to say, $10 million is still a nice payday and would afford my client financial independence. Unfortunately, his bad timing guess meant he missed the window of best opportunity.

I hope that this illustration will convince you to develop an Exit Plan for your business today. Set the clock for the number of years you think it will take you to put the company in a position to sell and achieve financial independence. That may be three years, it may be five years. By establishing a time frame, you can make a decision today which will propel you toward the day you will maximize your return. If you get to that target date and for whatever reason you elect not to sell, then don't sell. But reset the clock for another date and stay on top of your Exit Plan.

Without a disciplined approach to staying on schedule, happenstance rather than planning may end up controlling when and for how much your business will be sold. Remember, all buyers are looking for two elements in acquiring your company: good cash flow and upside potential.

QUESTION 3: WHY SHOULD I SELL MY BUSINESS?

Stop and think for a moment. What motivated you to start this business in the first place? I suspect that there were many personal and financial incentives that inspired you to become a self-employed entrepreneur. Among the most important was the prospect of wealth accumulation, i.e., the potential to achieve financial independence. During the course of starting, nurturing and fighting the day-to-day fires of any business, however, it is easy to lose sight of the goal of financial independence. I firmly believe that the day you start a business is the day you fix that goal in your brain and establish your Exit Plan.

Recently, I analyzed the age of my clients selling their businesses and was surprised to learn that the average was 45. I believe that most owners expect to be much older when they give up control and leave their companies. At one time, this expectation may have reflected reality. The last generation of business owners was greatly influenced by its experience growing up during the Great Depression. They were driven equally by their fear of having nothing and of losing everything. They were builders and savers. They were not spenders. How times have changed.

The current generation of business owners consists of baby boomers now entering their late 40s and early 50s. Unlike any previous generation, they came of age during a time of sustained growth and as a result have become the greatest "consumers" in the history of our country. They have worked hard but have consciously tried to balance work with play. Unlike their predecessors, this generation of business owners has adopted the "I can't take it with me" attitude and has included "lifestyle" on its menu of choices. More and more, baby boomers are choosing to sell now, taking their chips off of the table and adopting the lifestyle afforded them by financial independence. Many entrepreneurs are smart enough to realize that the best time to sell is when they can receive a premium purchase price and are still young and healthy enough to enjoy the fruits of their labor. I can assure you that none of these entrepreneurs has sold out and gone quietly into the night.

Unfortunately, time and time again I have watched owners postpone a sale only to find the obstacles they had hoped to avoid grow more intractable. I have observed that if a business owner reaches his early 60s without having sold his company, he probably never will.

For example, one of my clients told me that he planned to sell the company five years hence at age 62. He described all of the typical reasons he wanted to sell: more time with his wife, kids, church and volunteer work in the community. Suspicious of the delay, I asked him what he could realistically expect to sell the company for today. He stated that he could net $10 million after taxes and closing costs. This, clearly, would make him financially independent. I asked him why he wouldn't sell his company today. He believed that he was still too young to leave the company but felt confident that he would be able to do so five years from now. I cautioned him that if he procrastinated, he'd find it even more difficult to sell then than to sell today. He was surprised by my warning. He had not considered all of the ramifications of procrastination.

Unless you understand the sales process and commit to an Exit Plan, it becomes increasingly difficult for you to leave your business. If you are going to make this significant change, doesn't it make sense to do it when you can project another 20 to 25 years of good health? The longer you wait, the less time you have to relish this change.

I have observed many business owners resign themselves to the notion of "dying in office." "Why should I quit now? It is too late for me to do anything else with my life. I'll just keep coming to work." When asked what they would have done differently if they could do it over again, the answer is always the same: "I should have sold out sooner when there was more life ahead of me to enjoy and still sufficient time to develop a new 'me'."

When I shared this observation with the client I described earlier, he realized that he was concocting reasons not to sell when in reality that's what he truly wanted to do. Upon further reflection, he agreed that waiting would only make his decision to sell that much more difficult. He had mistakenly assumed that five years would magically change his attitude and give him the time he thought he needed to adjust to the reality of no longer being the business owner.

Within a year of our discussion, he was one of the first to sell to a publicly traded acquirer who was consolidating my client's industry. He has achieved the best of both worlds. He was acquired by an excellent company and he continues to function (in title only) as an officer of his former company.

As you can see, owners wrestle with these questions before they undertake the planning necessary to leave their businesses in style. The challenge to these questions lies in the honest assessment and critical reflection that answering them requires. If you fail to resolve these issues, you have erected a barrier to a successful Exit Plan. Viewing these issues in their proper perspective, as the mental and emotional groundwork for the Exit Planning process, will enable you to move forward on your successful Exit Plan.

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We, at The Exit Planner, *are happy to answer any questions you have about articles that appear here. We also appreciate suggestions from readers about the Exit Planning topics that they wish to see addressed. We welcome your comments regarding our newsletter. You can address your questions, comments or suggestions to: John H. Brown, President, Business Enterprise Institute, 650 S. Cherry Street, Suite 1100, Denver, Colorado 80222 (303) 321-2242.*

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