

WHAT IS MY BUSINESS WORTH?

**PREPARING TO SELL
YOUR BUSINESS**



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Introduction

Understanding the value of your business today will help you determine what steps may need to be taken to get the most for your business in the future. Ideally business owners should obtain their business value at least 2-3 years prior to the sale of their business to get the highest return on their hard earned asset. We realize that this may not always be possible however it can be highly beneficial.

Selling your business is often a once-in-a-lifetime experience. With just one chance to carry out one of the most important transactions in the business and the business owner's life, it's essential to make sure you get it right.

Determining your business value is a vital step in selling your business. No two businesses are identical. Unfortunately, many business owners delay obtaining their business valuation until it's too late, leaving the owner surprised at the value of their business whether less or more when it comes time to sell. If the value is less than expected, this leaves the business owner with very little time to work on increasing their business worth to meet their selling value goal. Additionally, with small businesses being sold at historic highs, the best time to consider selling your business is now. However, valuing your company's worth can be complicated, especially without prior experience.

Business valuation is more of an art than a science, and professional experience goes a long way in validating the determined value in the eyes of potential buyers. Business values are determined through formulas, a combination of strategies, positive positioning, storytelling, and additional assets, and there's no exact method to determine a number.

An accurate business valuation is only one piece of the puzzle when considering the sale of a business. The sale of a business is a process, not an event. The length of time to sell a business depends on the type of business, the appropriate pricing, the business income and desirability along with barriers to entry in your industry. This process can be a long and stressful one, with the typical length of a sale lasting 3 - 9 months. Luckily, selling a business is a routine process in the business brokerage world. There are specialized individuals that are highly trained experts that provide the experience, knowledge and resources to help you successfully sell your business.

In this Guide to Preparing for Your Business Sale, we're detailing everything you need to know for accurately valuing your business and preparing for your business sale. This comprehensive guide will answer the questions:

- What are the steps to prepare for a business sale?
- How are business values calculated?
- How can you maximize the value of your business?
- How do you make your business more appealing to buyers?
- How do you tell the story of your business?
- When should you work with a business broker?

To make sure you receive the maximum price when selling your business requires surrounding yourself with a professional team. Working with First Choice Business Brokers, a national leader in the business brokerage industry, will position you to receive the highest amount for your business, while taking the stress of the selling process off your hands.



Preparing to sell your business

In the business world, preparing for your business sale is referred to as 'positioning' your business. To position your business, you must ensure everything is organized, put- together, and ready to sell. These preparations include:

- Creating a planned selling procedure with a business broker
- Organizing your books and records to be clear and easy to understand
- Decluttering your physical business Depersonalizing your business
- Reviewing your A/P and A/R aging reports
- Clarifying the legal ownership of your business
- Cleaning-up outdated agreements with customers or vendors
- Updating outdated registrations or licenses
- Creating clear documents for current staff duties Preparing for a potential requested tax audit
- Preparing to disclose any potential litigation
- Detailing a business growth plan
- Contacting a professional business broker

In addition to preparing these aspects of your business, you'll also need to assemble all the necessary documents. Most buyers will not be interested until they have documents detailing the facts, finances, and figures of your business. Begin assembling the following documents when preparing to sell your business. These documents will also be requested by your professional business broker.

- Business Formation Documents
- Financial Statements
- Schedule C Tax Returns
- Corporate Tax Returns
- Statement of Seller's Discretionary Earnings and Cash Flow
- Building Lease
- Equipment Lease(s)
- Inventory List
- Equipment List
- Copy of Financing/Loan notes to be assumed (if any)



As you complete pre-sale work to position your business to sell, make sure to keep your sale plans confidential. Only share your intent to sell with necessary parties such as your CPA and legal counsel. It is highly recommended that you do NOT share your plans with staff members, even management. Regardless of your employee relationships it is critical that you do not share your plans until absolutely necessary. Your trained business broker will discuss this with you in detail. Making your intent-to-sell public can create uncertainty among employees, vendors and customers devaluing your business during this crucial time.

Potential buyers prefer that businesses come with low risks and high rewards. In fact, 1 in 15 small business buyers fail to close their sales, often due to backing out from too much perceived risk. To lessen the potential risks of purchasing your business, flag any additional areas of improvement within your business. These areas to review include:

- Legal condition – Ownership, licenses, zoning, and litigation
- Finances – Revenues, profits, taxes, and liabilities
- Business reputation – Image, publicity, advertising, and brand awareness
- Business operations – Staff, equipment, and business plans
- Transferability – Leases, documentation, organization, and training-level of staff

Reviewing these areas of your company will make clear the positive aspects that add value, as well as the less-positive aspects of your business that decrease value. Creating a detailed action plan of specific steps you intend to make in order to improve your company before your business sale can make your business more appealing to buyers. An experienced business broker can assist you in this process.



How to conduct a business valuation

Conducting a business valuation is the process of estimating the financial value of a business, including its profitability, assets, market value, and more. As valuation is not an exact science, analysts will also look at company storytelling, leadership, business plans, and other non-material assets to determine a business' true value.

Whether you're looking to sell soon or just getting ahead of the curve, it's always a good idea to have regular business valuations, so you're ready for whatever the future may hold. Of course, if you are looking to sell your business now, a business valuation is an essential piece of the puzzle to successfully selling your business for the highest value in today's market. Without a professional valuation providing a realistic value, sellers may miss out on potential offers from qualified buyers.

When analyzing a business value, in the mid-market there are three main strategies that professional business brokers and investors use. These strategies are **comparable analysis**, **precedent transactions analysis**, and **discounted cash flow analysis**. For mainstream businesses the most common valuation method is utilizing the **earnings multiplier method** which is using recently closed transaction sale multipliers of the seller's discretionary earnings (SDE).



COMPARABLE ANALYSIS

is a valuation method that measures a business' value by comparing it to other businesses in the same industry. Comparable analysis uses financial data from earnings



PRECEDENT TRANSACTIONS ANALYSIS

looks like comparing one's business to other businesses in the same industry that recently sold. This gives an idea of what a certain type of business is presently selling for, which can be a good starting point. However, this business valuation method must be updated regularly to be most accurate, as it regards current industry trends.



DISCOUNTED CASH FLOW (DCF)

analysis measures a business' value based on expected profitability or future cash flow. This method is preferred by many investors to judge whether they will receive a return on their investments.



EARNINGS MULTIPLIER

this method utilizes recently sold comparable data of multipliers of seller's discretionary earnings (SDE) in the same industry. A Market Price Analysis provides the most probable sales range options utilizing sold comparable data, multiples of SDE, multiples of EBITDA and multiples of revenue and industry profit margins.

In addition to these valuation methods, other aspects of business value include tangible assets, intangible assets, financial metrics, and any business liabilities. Tangible assets include material goods e.g. furniture, fixtures and equipment, tenant improvements, property and inventory. Intangible assets include brand awareness, brand recognition, trademarks, and other in-material assets that add value to your business. For example, in higher value mid-market businesses, good brand awareness can increase a company's revenue by an **average of 23%**, making the business a more valuable entity.



In addition, financial metrics that add to your business' value include financial statements like profitability margins. On the flip side, any liabilities such as excessive debt may decrease your business' value.

All of these factors and more go into assessing a business in its total. As you can see, these methods give a best-estimate of a business' value, and there is no one true value for any given business. Nonetheless, there are calculation methods for a more science-based business valuation approach, which are discussed below.



How to calculate the value of your business

Given that a business value depends on many factors like revenue, profits, size, and expected growth, there are a few calculation methods that professionals use to conduct business valuations. While these calculations still do not give a singular, exact answer, they can give an excellent estimate and add legitimacy.

SDE

The seller's discretionary earnings (SDE) method is a common calculation for business valuation. The SDE gives a clear number of a business' income prior to the owner's salary deduction and other non-operating expenses. SDE is a popular tool for smaller businesses.

To calculate the SDE, add discretionary expenses to your business' net income. The SDE figure can then be multiplied by your industry's multiple to give an estimate of its value within your specific industry.

EBITDA

Similarly, the EBITDA calculation gives a tangible number for a company's true earnings. EBITDA stands for earnings before interest, taxes, depreciation, and amortization. EBITDA is more common for larger businesses with gross annual sales above \$1 million USD. However, the EBITDA alone may not tell the whole story, which is why it's common to calculate EBITDA multiples.

EBITDA Multiples

The EBITDA multiple is another common method for calculating business value. This method may provide a more accurate picture than solely the EBITDA value as it takes into account assets, shares, growth potential, and other valuable aspects of a business. The higher this score is, the more valuable a company is.

To calculate the EBITDA multiple, you use the calculation:

- $\text{Enterprise Value} / \text{EBITDA} = \text{EBITDA Multiple}$

This calculation shows the ratio between a business' annual EBITDA and its enterprise value (EV), or total value of the company. While this method allows for a fast evaluation, it may not be a good representation of cash flow. This calculation is best for larger organizations.

Comps Method

The comps method is another method for calculating your business' worth. This method entails comparing your business' trading multiples, such as your EBITDA multiple, to other recently-sold companies' multiples. This is an excellent strategy for smaller businesses to demonstrate their values within their markets.

To access the multiples of recently-sold companies, you can consult a broker or public financial forums for public sales. Note that the average cash flow multiple for businesses sold in 2020 was 2.28.

While the above calculations are helpful in estimating the value of a business, they don't always paint the full picture. To find an accurate valuation, you can partner with a qualified business appraiser like First Choice Business Brokers.





How to get the maximum value for your business

While being overly optimistic often leads to disappointment when it comes to selling your business, there are ways to maximize the value of your company. It's important for sellers to be realistic, **as over 50%** of lower middle market transactions fail to be accepted, often due to seller-refusal to accept lower-than-expected offers. With this in mind, continue reading for some concrete methods to increase the value of your business.

Increase company performance

One of the best ways to increase your business value is to put work into increasing company performance before you sell. Analyze your company's profitability and decide what quick and long-term fixes can be done to increase this. Depending on your company size, hiring an interim CEO may be a smart solution to quickly increase revenue.

In addition, establishing a plan for growth can add value to buyers even when those issues aren't yet fixed. This provides buyers with a clear pathway for increasing profits on their potential investments. Overall, increasing your business' profits will lead to a higher EBITDA multiple and, thus, a higher selling point.

Tie-up loose ends

As mentioned earlier, positioning your business includes tying-up loose ends. This includes decluttering your business, clearing debt or litigation issues, renewing necessary permits or licenses, clearing-up outdated contracts or agreements, establishing legal ownership, and more. Having a 'clean' business, both physically and on-paper, will increase your business-value in the eyes of buyers.

Organize financial statements

In addition to tying-up loose ends, having organized financial statements is a must to maximizing your business value. This makes everything the buyer needs to know about your finances clear, helping to eliminate any uncertainty. Make sure your financial documents are accurate and up-to-date.

Add competition

Another method for maximizing your business value is to create competition. If more than one buyer is eyeing your business, it appears to be, and likely is, more valuable. In addition, more than one interested buyer increases demand, thus increasing your business value and likelihood of competing offers. To add competition, present your business sale to all possible buyers through a qualified business broker.

Tell the story of your business

Having a successful business sale often comes down to storytelling. Telling the inspiring story of the start of your business, including the potential future story, helps to persuade buyers to be interested in your business and view it as valuable. Keep reading below for details on how to tell the story of your business.

Work with a broker

Partnering with an expert business broker like **First Choice** ensures your business will be in the best possible position to sell. Business brokers help you find your business' points of improvement, organize and position your business, arrange financial documents for buyer review, find the best buyers, and maximize your business' selling price.

Some business owners write a lot of their personal expenses through their business and often these items are not easily identifiable to a potential buyer so therefore the seller will not receive value for those dollars even if the business provides that income. There are also situations that certain expenses are acceptable and not an issue. An experienced business broker can provide guidance on what is typically acceptable by would be buyers and/or their lenders.

Shift your mindset

It's important to be objective and realistic when selling your business. Holding onto an image of your ideal buyer, a strict selling point, or a desired business-legacy can hold you back from great business deals. Having tunnel-vision on a desired outcome can also blind you from necessary changes that need to be made in your business. Rather than focusing on a specific price, focus on building a worthy business that you're proud to display to buyers.



How to make your business appealing to buyers

In addition to maximizing your business' value, making your business more appealing to buyers will result in a better sale. In the market of over **30 million small businesses in the United States**, with only **30-40% of businesses actually selling**, you'll need to make your company's worth stand out.

Cater to your buyer

Different buyers value different business aspects, as well as use varying tools to determine the worth of a business. For example, some buyers might use the SDE method to determine business value, while others prefer a comparison analysis. Catering your business-positioning to your buyer's preferences will instantly make it more appealing.

Do the work for your buyer

Also, doing much of the hard work for your buyer(s) makes the purchase less intimidating. This may include getting necessary documents in order, having clear and organized accounting and financial documents, providing a detailed business plan, providing a clear sale and transfer plan, and other steps to make the process easier for your buyer. Experienced business brokers like those at First Choice have transition forms that can help guide you and the buyer through pre and post closing items.

Be honest

Another way to make your company more appealing is to be up-front about any potential issues. While you may be tempted to hide the down-sides of your business, revealing them from the start will actually build more trust with buyers. In fact, during the due diligence process of a sale, **50% of deals fall apart due to finding undisclosed issues**. Every buyer knows that there could be hidden negatives or risks when acquiring a company, so hiding issues will likely be counter-productive in the long-run.

Transfer leadership in advance

Furthermore, establishing a second-in-command employee or manager makes a potential acquisition much more appealing to buyers. Buyers will be less apprehensive about the transition of ownership knowing that they will have a knowledgeable, experienced individual on their team from the get-go. Completing these steps, as well as wisely positioning your business, will leave you with a very appealing business for sale.



How to tell the story of your business

Successfully closing a business sale often comes down to storytelling. Storytelling in this case involves embracing the human element of business. Your business story should help the buyer have a clear vision for the future, show them what it would be like to be a part of that future, and reveal why acquiring your company is the right choice. At the end of the day, business is less about figures and more about people.

To tell the story of your business, show the problem that your business solved, demonstrate how this has helped people, reveal your modern success, and touch on what the future could hold. The basics of a business story include:

- A main character
- A challenge the character faced
- How they overcame that challenge

Your business story does not need to be over-the-top or revolutionary, but rather bring a bit of humanity to the numbers you're providing. Make sure to remain authentic and honest as you're trying to build trust with your buyer.

Business-owners may also partner with a brokerage professional to learn to effectively portray the story of their business. When working with a First Choice business broker, you will have a consultation process to get to the root of your business' story. First Choice can then help you weave together an engaging story and marketing materials that will motivate your buyer to move forward.





When to work with a broker

Selling your business is a large responsibility to carry out on your own. Although business owners can execute this process alone, working with an experienced business broker expert can make the selling-process easier and increase your selling price. A professional business broker helps validate your business to buyers.

Working with a business broker like First Choice gives you in-depth analysis of your market, helps you best-position your business, provides you with an accurate business valuation, assists you with negotiations, and guides you through the sales process to closing.

If you do decide to sell your business independently, your business is considered as 'for sale by owner' (FSBO). You may want to choose a FSBO sale if:

- You cannot find an interested or compatible broker
- You cannot afford the broker's fee
- You want to have full control of the sale process
- You have your own professional experience with selling

Working with an experienced business broker like First Choice may be the best option for your company if:

- You have never sold a business
- You own a small business
- You are not sure what your business is worth
- You want to get the maximum value for your business
- You want to have an efficient, successful sale
- You want to avoid legal complications
- You need a third-party to facilitate the process
- Your business is in a U.S. state that requires a business broker to be licensed
- You are having trouble finding potential buyers or don't know where to start

Working with a broker also allows you to focus on running your business while they streamline and manage the selling process. Brokers have extensive experience in closing sales, and they help you with all financial, operational, and legal proceedings required in a business sale. Although brokers receive a commission, they may help you reveal assets and add business-value to have a higher selling-price than imagined.

Overall, working with a business broker helps you manage the long, stressful process of selling a business while optimizing your outcome. A broker like First Choice also helps you find the best buyers while keeping your sale confidential, safe-guarding the value of your company during this crucial time.



Conclusion

Though often once-in-a-lifetime for small business owners, selling your business may be the most important, and most difficult, step of your business-ownership journey. With all the steps of this process, market competition, and lack of experience, selling your business may seem overwhelming.

Luckily, First Choice Business Brokers helps business- owners around the nation successfully sell their businesses. We bring the experience, expertise, and resources you need to carry out your biggest business endeavor yet.

You deserve to have an excellent business-selling experience. Contact us today to learn how First Choice Business Brokers can help you get the business outcome you desire.



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