CLOSING THE DEAL

A **BUSINESS OWNER'S GUIDE** TO AVOIDING PITFALLS, DISPELLING MYTHS, AND SELLING YOUR BUSINESS THE RIGHT WAY

ANDREW CAGNETTA

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INTRODUCTION

Owning a business comes with many challenges, no matter where you are in the life cycle of your business.

When you're getting started, it can be a struggle just to pay the bills. Every day, new business owners worry about getting clients and then meeting their needs, often while wearing just about every hat that comes with the business.

Once you're up and running, it's a constant battle to grow your business. Getting new clients and keeping the ones you have. Managing costs and increasing profits. Hiring staff. Figuring out how to work on your business, not in it.

Then there's the exit strategy. When do you want to get out? How long in advance do you have to plan? What steps do you need to take? How do you get the maximum value, to make your investment of all that time and hard work really pay off?

That last question is the most important. And for most business owners, it's the hardest one to answer. Believe me, I know. Long before I entered the world of business brokerage, I struggled with selling my own business and trying to buy a new one. It wasn't a great experience, and it wasn't very profitable.

But it ultimately led me to this field and to Transworld. Over the past 25-plus years, my team and I have helped thousands of business owners get the right answers when it comes to selling their business. More important, we've helped them get the right deal. In many cases, we've spent much more time helping them get their business ready for sale than actually selling the business. There's a reason the company is called Transworld Business Advisors, not Transworld Business Brokers. We sell businesses, but advising and educating are probably the most important part of what we do.

That's what led to this book. By sharing my own experience, and interviewing experts in other key areas who can share valuable insights and information, this book can be one-stop shopping for any business owner, whether you're close to selling or just beginning to think about a timetable.

Your business is more than just your job. It's your baby. You've nurtured it. You've struggled through the growing pains. You've invested a lot of sweat equity.

You want that investment to pay off. You need that to happen. This book will help make that possible.

CHAPTER 1

MEET ANDY CAGNETTA

I can certainly relate to the thousands of business owners I've worked with. Not only am I a business owner myself, I've pretty much always been one. I began my entrepreneurial journey right out of college, in the New York City area. I sold cellphones and started my own business, then moved on to guitars and lighting and then bought a pasta shop with some family members in Hartford, Connecticut. My wife is from South Florida, and she really wanted to raise our kids here, so after selling the pasta shop, we moved south.

I set out to buy a business here, and it was a frustrating experience. I didn't know business brokers even existed, since I had sold the Hartford business on my own, but they were advertising businesses for sale in the newspaper when I searched in Florida, so I met with them, and I was not impressed. They made me feel like I was dealing with the stereotypical used car salesman.

But then one day I met with Don Parrish and his wife Bonnie, the owners of Transworld. We clicked, and they invited me to join the company. I did, and fell in love with the business. I did well in my first couple years, then Don was ready to retire. I bought the company in 1997, and it's been growing ever since.

Growing this company took a lot of hard work and a little bit of good timing. In 1999, we had an opportunity to take on some growth capital with a company that is now known as NewTek. Their CEO is one of the people interviewed for this book. Back then, they were involved in something called a Capco program, which was a state-sponsored opportunity for businesses to invest in local businesses.

They looked at Transworld and decided to give us $3 million in growth capital. It was actually based on a dot-com rollout we were going to do. But by the time we secured the money in 2000, the dot-com world came crashing down, so the rollout didn't happen and we couldn't use the $3 million. But 10% of it was contracted for use to grow our business, and they told us to use that $300,000 for that purpose.

So that's what we did. We opened some bigger offices here in Fort Lauderdale, and then we started acquiring some business brokers across the state of Florida through some joint ventures. By 2003, NewTek had gone public and they weren't fans of our business because of the unusual cashflow it has in closing deals and not closing deals, so we bought them back out.

As we built out Florida, eventually having 10 offices throughout the state, some were in places like Jacksonville and other areas that were hours away from my office in Fort Lauderdale. As a result, it became more difficult to handle things like employees and repairs and lease issues. We didn't have time to drive five hours to talk to people, and we knew how difficult it would be to jump on planes to places like Atlanta and Charlotte, and cities further away, to hire people and work on locations and everything else involved.

So, in 2010, we decided to franchise. We partnered with United Franchise Group to take it nationwide. We're not in every state, but we're in most, and we've become a worldwide brand, with offices in 10 countries outside the U.S.

I believe when it comes to business brokerage, size matters. Yes, there are a lot of individual brokers out there who are very good at what they do. But being part of a bigger organization is becoming more of a trend. For one thing, it's increasingly hard to operate a business because you need so many more things. Years ago, my office could consist of me along with two or three other people, including a secretary. We advertised in the newspaper and we closed deals. It was pretty simple. But now there's so much technology involved, from the computers to the software to the digital marketing and the social media, and you have to deal with litigation issues and insurance needs, and I think that's really hard to do as an individual broker or a small brokerage office. What's interesting to me is how many brokerages have decided to cease being independent and come on board with us at Transworld. That gets us brokers with a wealth of experience, and it gets them the power of a huge company.

Size doesn't matter when it comes to the type of business we work with. We sell small businesses that could be valued at

$50,000 or even less, and we work with businesses that are worth $50 million and even more. In fact, that could be our tagline, 50 thousand to 50 million and everything in between.

And they cover all kinds of industries. I've sold several psychology practices, which is about as personal as it gets. We’ve sold numerous medical practices along with medical manufacturing and distribution companies, not to mention a wide range of manufacturing companies. We’ve done a lot of service businesses such as landscaping, pool and pressure washing, painting, and the construction industry, including contractors and subcontractors, window and screening companies, drywall companies and framing companies. There are retail businesses such as dry cleaners and clothing stores, all types of restaurants, advertising agencies, and the digital world. We estimate that we’ve sold more than 10,000 businesses, mostly independent but also our fair share of franchises.

People often ask me when is the best time to sell a business. I always say, “When you don’t need to.” The best time is when you’re not pressured into selling. Unfortunately, things happen that force people to sell. What we call the “Bad D’s” come into play all too often. Death, divorce, disagreement and disability happen, and people find themselves in a position of needing to sell, which means they don’t have the time to run the proper process and get the best offer possible. They don’t know the true value of their business. They’re not in a position where they can take their choice of buyers.

But the good news for people like that is, depending on the market and other factors, as long as they've avoided some of the common and costly mistakes business owners make, they can still get a good price. Pointing out those mistakes and helping business owners change their ways is a very big part of what we do. I like to think of us as not just business brokers, but business advisors, and the advice we give can pay huge dividends.

For example, something we've told countless business owners is, "Keep your eye on the ball and the pedal to the metal." That's because one of the biggest mistakes someone can make is say, "Okay, I'm going to sell my business in a few years, so I can start taking it easy." No, they need to keep working as hard as ever, if not harder, to continue growing the business. Because if you coast just a little, revenue goes down and so does the value of your business.

The same thing happens when business owners get too involved in the sales process too early. Again, that takes their eye off the ball and the value of their business suffers. That's why we're here. Our job is to help them sell their business. When we need answers to questions, or need them in a meeting, we'll let them know. In the meantime, stay focused on your business.

I realize I'm biased on this one, but obviously I believe you should not go it alone when you sell. You can't just list your business on a "business for sale" portal and sell it in a month. When you do make the decision to sell, it could take a year or longer to make the necessary changes in order to get the maximum price when you sell.

Some are easy fixes, like a building cleanup. Some take longer, such as getting your books in order, or correcting things that a buyer will see as a potential risk, such as one customer providing 80% of your revenue, one supplier providing 80% of your materials, or the owner wearing way too many hats. A good business broker knows what to look for and can tell you how to eliminate the potential deal killers.

We can also handle whatever challenges come along. There are many common challenges, such as insurance issues, which is becoming a bigger challenge as things like cyber fraud and climate change are affecting insurance rates. We’re having to find people deep inside these insurance companies to get things transferred or a new policy written. It's actually quite interesting.

Sometimes what starts out as a common challenge becomes unique. For example, when a business owner rents their building, they need their landlord to sign off on the deal when they sell their business, because now there’s a new tenant on the lease. One time, that landlord happened to be a sitting U.S. Senator. It’s never easy to get ahold of someone like that, but in this case, we called the property management office, and they said, “The senator is out of town and we can’t get in touch with him for a week.” I said, “Well, this is headline news because here’s a U.S. Senator and his own people can’t get in touch with him for a week.” As it turned out, the owner of this business and the senator had gone way back, so eventually we were able to get word to the senator that we had this issue, and he was able to sign the documents for us.

In another instance, we had a landlord that was refusing to work with us. I looked to see where they lived, and because I had a pretty good sense of their religion, I speculated on their house of worship, and called a friend of mine who I thought would be in that same congregation. He said, “Of course I know that person.” He agreed to set up a meeting for me, and came along to the meeting, and after a conversation the landlord said, "Okay, Andy. You're a good guy. How can I help you?" Sometimes it takes a little extra creativity to get the job done.

Whether a business owner owns or rents their property often depends on the type of business and their location. If you have a manufacturing business, you probably want to own. Here in Florida, about 90% rent. My advice is if you want to be flexible and be able to grow, you’re going to want to rent and move on to different facilities.

I’ve given a lot of advice to a lot of business owners over the years. Which brings me to this book. As Sy Syms said, an educated consumer is our best customer. So, we want people to understand the process. Not being educated in the process slows things down and keeps people from getting deals done. I have a current client who’s a good friend, but he won’t give me his financials unless his attorney and CPA both agree to it, and getting their approval is delaying things.

Even though he's known me for years and trusts me, I still can't get him to realize I'm not going to just hand his tax returns to anyone who walks through my door. That information will only go to a serious and qualified buyer. In the meantime, he's telling me, "Just find a buyer," and I'm telling him, "I can't do that because I don't know what they're buying." He owns multiple restaurants and he wants to sell them for $7 million, but without the financials, I can't determine if that's a good price.

The information in this book will help people like him say, "I get it now. I understand the process and know what I need to do to not just sell my business, but get the best price for it."

So, what type of business owner should read this book? Someone who's thinking, "I'm going to sell my business next year"? Someone who's thinking, "I'm still a few years away from selling"? Someone who hasn't started thinking about a timeline for selling their business?

The answer is, "All of the above." Every business owner needs to be ready to sell. Every business owner should know what's involved in the process, and what can either help or hurt their prospects when the day comes that they do sell.

Your business didn't come with a "how to" guide. You've had to learn a lot on your own about how to run it and build it, often by trial and error. Think of this book as your how-to guide for when you sell, whenever that may be.

If you should happen to come up to me one day and say, “Andy, I read your book six months ago,” I hope you finish the sentence this way: “…and I’m ready to sell. I feel confident that I have everything in place, and I want to thank you because I found some things that needed cleaning up and I did that. I talked to my attorney and my CPA and my financial advisor and my family, and I’m ready to go.”

So let’s get started.

CHAPTER 2

THE RIGHT DECISION AT THE RIGHT TIME

Selling a business is a huge decision. It could be the number-one financial transaction of your life and should be approached and treated accordingly. It is serious business and you must take due care when it comes to the process.

But first, you must commit to the end game. If you want to sell, then commit to selling your business, not just testing the market. Selling your business is like any business endeavor, it is fraught with pitfalls and risk. Therefore, it should only be undertaken if you are serious about the outcome.

A serious seller knows what he or she is going to do after the sale. So, get yourself organized, draw up a plan and commit with conviction to your decision. If you have partners, get them to buy in and hold you accountable throughout the process. Do not tell your employees (we'll tell you why shortly). Do not tell anyone who is neither an owner of your business nor your immediate family/spouse of your plan to sell. You may consider meeting and conferring with close advisors like your accountant, lawyer and investment advisor as we will need this team of professionals throughout the process.

Now is the time to plan the cruise around the world or whatever is on your list of things you want to do with the proceeds of the business sale. Why? Because you will experience seller's remorse at some point during the process. In order to overcome that emotional response, you will need to remember and revisit your initial decision to sell, have future plans, and have others holding you accountable to that decision.

Your reason for selling is a critical component of the sale. It is often the first question most buyers will ask. If your answer is wishy washy or unclear, a buyer's suspicions will be raised and could prevent a sale. Your answer to the question "Why are you selling?" needs to be concise, real, believable, consistent over time, and ingrained into your head.

Frankly, as important as this is for the buyer, it's just as important that you believe and commit to it as well.

Selling a business is often a tough road. There will be many junctures when you'll consider just quitting the process altogether. You must be committed and willing to walk blindly through risk, frustrations and danger along the way. That is why you will need your team of advisors that will hold you accountable.

Now that your commitment is solid, let's talk about getting through the process unscathed as a result of the aforementioned dangers and risks!

Keep It Confidential

Before we move on, let's talk confidentiality. Who needs to know about your decision to sell?

No one.

That may be too sweeping of a statement, but in reality, only your closest confidants need to know about the impending sale. The more people that know, the greater the danger of the wrong people finding out. Who are the wrong people?

- **Your Employees** – with very few exceptions, you should not share your plans with employees. They get overly concerned with what will happen to them after the sale. We have seen many employees leave due to this concern, which is strange as most buyers value the established employees highly. They are part of what the purchaser is buying and the buyer often gives them incentives to stay once the transaction is completed. Your best bet is to wait till after the sale to speak with any employee.
- **Your Competition** – This is obvious as you do not want to give your competitors the ability to use a pending sale as a tool to take business from you. The exception to this is when a competitor is seen as a good buyer. In this

case a strong nondisclosure agreement (NDA) is essential.

- **Vendors and Suppliers** – Don't tell them. Period. We have seen suppliers and vendors change credit terms or limit purchasing incentives due to fear of payment issues. Dealerships and exclusive contracts that drive value may be an exception. Hopefully, these types of arrangements are in writing with assignment clauses that will be an asset to a business deal.
- **Customers**- Absolutely don't tell them. You do not want revenues to drop during this sale process. If you have a customer concentration issue, say 20 percent or more of your business is from one customer, we may eventually have to get their buy-in to the process to be able to sell at full value.
- **Advisors** – Accountants, attorneys, investment advisors, bankers, business coaches could be good people to have in your small circle of those who know you're your plans. Some of those very same people may have advised you to sell. Just understand, if any of these advisors will be losing your business, they may put their interests ahead of yours. Also, if they are unfamiliar with the process, they could give you bad advice regarding valuation, tax issues, or deal structure, which could lead to killing a deal. Third party interference is a huge issue in transactions.
- **Landlord** – We have seen this go both ways. The best advice is to understand your lease assignment rights. If you need a new lease or an extension, it may make sense to work with a friendly landlord. If you have

plenty of time left, then you should wait until you have a deal in place to inform your landlord.

- **Family** – This is tough. Your spouse clearly needs to know. Your kids may not. Certainly, if they are partners or have a stake in the business, are integral to the future of the business, or have been promised the business in the past, you may need to have that discussion before you put the business on the market. But our simple advice is, if you have the ability to sell the business without their permission, don't tell them.
- **Everyone Else** – Loose lips sink ships. It's only natural to want to tell people. But keep the process private and close to the vest. Even if you have a deal in the works, it can still fall through. Talking about it is bad luck and dangerous. A deal is done when the papers are signed and the wire hits your bank account. Even then, there may be obligations still to perform and monies yet to be paid. Keep it on a need-to-know basis.

If people do find out, you have a few choices including lying to them, but sometimes the best tactic is diversion. If you hire Transworld, we have an M&A division and a franchising division. Simply tell whomever that you are looking to expand in the future and Transworld is leading that effort. If they have a few million dollars, and want to invest in the plan, they can be included in the process. That will usually shut down the inquiry and scare off the nosy folks. Or perhaps tell them you are seeking new insurance or even a line of credit. That way you can have several meetings with prospective buyers and pass it off as bankers or insurance adjusters.

CASE STUDY – KEEPING THE SECRET

We listed a niche business for sale which was one of just two knife distributors in the country. If we went to the marketplace and advertised "knife distribution business for sale" in Florida or even the southeastern United States, everyone would know who it was. Instead, we advertised a "Camping Equipment Distribution Business." Our strategy worked well, even though the eventual buyer was the one and only other competitor after our client passed away (the original reason for sale was the seller's medical issues). But vendors and customers did not find out prematurely about the sale and the widow was able to receive full value for the business.

CHAPTER 3

WHAT'S IT WORTH?

Let's tackle the big issue right now, up front. Every business owner has thoughts and aspirations of what business sale proceeds will be, and most are disappointed when faced with the reality of their business value in the marketplace.

At the end of the day, your business will be worth a multiple of your earnings. For the purpose of this book, let's focus on businesses that have an EBITDA of less than $1 million. *EBITDA (Earnings Before Interest Taxes Depreciation Amortization) is a widely used metric of corporate profitability that makes it easier to compare companies.*

When we are talking about this category of small business, we talk in terms of seller's discretionary earnings (SDE), which is EBITDA plus one owner's compensation plus benefits. SDE is also referred to as adjusted net, discretionary earnings, seller's discretionary cash flow (SDCF), and owner's benefit. The terms are most often interchangeable.

Understanding Market Value

The calculation of SDE is subjective. But handled by an experienced business broker/intermediary, it should be done so your SDE is comparable to other businesses for sale. And once this SDE is properly calculated we can then determine a most probable market value for your business. This is not the same as fair market value that a true business appraiser who does a USPAP level certified valuation on your business may report. This is most likely a business intermediary's estimate and is a value most often based on comparable sales in your industry.

So, what multiple of SDE will your business sell for?

Two times.

Maybe three, perhaps a stretch to four, but it could also be as low as one. Disappointed? Don't put the book down just yet. Let's talk a bit more about the reasons why your business may sell for more or even less than that.

Business sale multiples are driven by the quantity and quality of your earnings.

Quantity of earnings is easy to explain. If your business makes less than say $75,000, it is inherently riskier to buy. If someone buys your business and makes a $100,000 mistake in the first year, they most likely will go out of business. Therefore, a business with minimal SDE may only sell for one-time SDE. Now if your business has an SDE of $750,000, and a buyer makes that same $100,000 mistake, they may have learned an expensive lesson, but most likely will not be put out of business. Therefore, small businesses' SDE multiples range from one to four for businesses that earn less than $1 million EBITDA (and let’s say SDE too) based on the quantity of the SDE and resulting inherent risk associated with the amount of SDE.

Now that you understand the quantity variable, let’s talk quality. Quality of earnings will definitely have upwards and downwards pressure on that “two” multiple. Quality of earnings will be determined by the business buyer’s belief that the profit was not a fluke and will remain and continue to grow into the future with a new owner at the helm. Here’s a list of items that can add to quality of earnings:

- Past years earning trends. Up, flat or down?
- Quality of books and records (more later)
- Customer base diversification or concentration
- Industry trends
- Location
- Employee skill and longevity
- Brand and other intellectual property
- Goodwill
- Asset value
- Ease of transfer
- Competition levels
- Ability to finance the transaction
- Potential
- And much more

So, back to the original question. How much can you expect to get for your business? No one truly knows until a buyer pays the price at a closing table. Business valuation is an art, not a science. It is rare that two business valuation experts agree when presenting formal reports. Want to see this in action? Go to a civil court and watch partnership disputes, divorces, and taxation matters being disputed by two wildly diverging valuation "experts."

Are there outliers? Sure. We can all think of businesses that have sold for crazy multiples and huge prices without having any earnings at all. Your business could be an outlier, but more than likely it isn't, and you have to stick to this formula.

So, if your business is going to be sold for a one to four multiple of earnings, why not stay for a few years and make the money you would earn in the sale? Good question. Back to your commitment. Why are you selling? Life's eventualities such as sickness, partner dispute, burnout, relocation, cash flow issues, or leadership inadequacies will all trump the ability to be patient and wait out a result. Additionally, you run the inherent risk of seeing your business devalue, or even go out of business. If you can stay and are willing to risk the wait, hang around and make your money. Otherwise, if you need to sell, then accept your valuation and start the process.

CASE STUDY – THE PRICE ISN'T RIGHT

We had a listing for a small Vape business owned by a sharp and smart young entrepreneur who felt she knew her business. She had over 100 "unique flavors" and was very proud of the business she had grown. We did a valuation, and with her SDE of approximately $62,500, we determined the value was around $127,000 and suggested an asking price just above that number. She insisted that she would not list it for under $800K as the variety of flavor combinations was proprietary and would be sought after by the industry. We listed it at her requested price, but after a month of no action from our marketing channels and complete sticker shock and indignation from industry buyers we approached, we told her we needed to reduce the price. When she refused, we decided to take the business off the market. Shortly thereafter the business closed due to her personal issues that forced her to sell in the first place.

Revenue Reality

Now that we have tackled SDE multiples, we should talk about methodologies that use revenue comparables and the tangible and intangible asset value of your business. First, let's talk about revenue comparables. They are a great way to compare businesses and calculate value. SDE multiples rely on consistent adjustment and calculation. This is sometimes performed inconsistently by business owners, accountants, and intermediaries. This is also somewhat of an art, therefore subject to opinion and error. Revenues are better reported and more consistent as nothing needs to be adjusted. Herein lies the issue: What happens when a business has great revenues, but loses money? Unless there is a way for a buyer to realize a profit, the business may not have any value beyond liquidation value. For example, who wants to buy a business that grosses $2 million and loses $200,000 a year? Revenue multiples are good for benchmarking, but the bottom line eventually comes back to earnings.

What about asset value? Value of inventory, furniture, fixtures, equipment, customer list, website, etc. If the assets do not drive profits, they are worth a liquidation value that can be less than the original cost. We do sell a lot of businesses for “asset value” when they are not making money. For example, a restaurant location with plumbing, electrical, fixture buildout ready for a new owner/concept does sell. However, it is most often for a percentage of the original value. We see that percentage vary, but a good start is 25 percent of original cost of the assets and buildout.

So then, what assets are included in this most probable selling price (MPSP) calculated using the above methods? You can expect furniture, fixtures, equipment, inventory (a reasonable level) and all intellectual property such as trade name, website, phone numbers, etc. to be included in any sale. Cash, accounts receivable, deposits are not usually included. If accounts receivable are significant they can be included later if necessary. And all of these assets must be delivered free and clear of any liens or liabilities.

With all that said, could your business sell for more? Sure. But most likely the increased value will be driven by some outlying factor that is strategic in nature, thereby making it valuable to a buyer. A strategic or synergetic buyer might be able to capitalize on your business assets better than you could due to access to resources that you do not have. Earlier we emphasized the word potential as a factor of increased multiples. That could drive your business value higher, however, when people buy businesses because of their potential, it isn't usually reflected in the price they pay. That is their return on investment, not yours.

Lastly, what will get you the best price? Competition for the deal. You need to have several buyers looking to purchase your business simultaneously. How do you achieve this in the marketplace? By having the right buyers engaged and having the proper information to decide to buy. That is only accomplished through the right broker that properly exposes your business to the marketplace. More on this topic later.

Will Your Business Sell?

No one can say with 100 percent certainty. We do know one thing though. To find the right buyer, one who is willing to pay a price that is acceptable to you, and then get the deal done, it takes an incredible amount of expertise, determination, marketing, and a bit of luck.

Finding that right buyer is often like finding a needle in a haystack. Having a company with the ability to confidentially market your business to tens of thousands of buyer prospects is critical to the process of finding the right buyer at the best price.

We also know that it will take a minor miracle for you to navigate this process on your own. We often liken it to landing a big fish. You may be lucky enough to hook one, but getting it in the boat is a whole different story. You can lose that fish for many reasons, most of them having to do with inexperience and lack of expertise.

If having the right price and terms ups your chances of getting to eat that fish, then just getting it in the boat is not enough. You must properly clean and cook the fish to have a great meal. If you're an expert at valuation, packaging, marketing, deal structure, negotiations, due diligence and closing deals, by all means have at it and take a crack at selling that business yourself. Otherwise, hire the right broker.

Even with all that said, many businesses never sell. There are many reasons that a business might not sell. We've tried to highlight most of the major ones so you can avoid the glaring mistakes that cause a good business not to sell.

Who is the Buyer?

The majority of the time, the buyer for your business is an individual, someone buying a business to replace an income or seeking to take a shot at living the American Dream. And this is a great time to sell. Currently in the United States, SBA loans can go up to $5 million with as little as 10 percent down. This is a huge advantage for business buyers and sellers that can qualify, and when we talk about buyers who are able to leverage up to $5 million in purchasing power, that covers most small businesses we're discussing in this book. We'll talk more about financing a little later.

Most business buyers are first-time business owners looking to buy not only a future income, but a turnkey business, replete with all the assets needed to run the business. They will need training and guidance from you the seller. Since they have none of the assets nor the knowledge/experience necessary to run your business, they often pay the most money.

There are times when another company will buy your business. If it is a competitor, they usually do not need all your assets, and therefore will not usually pay full value for your business. Sometimes a company could be strategic or synergistic and will pay more for your business because you are a missing piece of their future business plans or fulfill a specific need from which they can gain economies of scale. This type of buyer is rare in the small business arena we have been discussing.

Private equity groups are another type of buyer. They are investor-backed pools of capital that purchase businesses. Their minimum criteria usually include businesses with at least a $1 million EBITDA, more often at least $2 million.

However, once they own a specific type of company, they could seek “add-ons” within that company’s industry.

But again, these types of purchases are few and far between. And even if your company is a target of this activity, other companies/private equity groups are professional and meticulous buyers. Unfortunately, they’re not often the best payers.

We estimate that over 90 percent of small businesses are bought by individuals. Some of these buyers can be immigrants from other countries seeking a visa to work and live in this country. Don’t believe the myth that these immigrating buyers will overpay for your business. People who immigrate to this county are often doing so after being successful in their home country. Regardless of how difficult it can be to make money here in the U.S., being successful in other countries is often tougher. Therefore, the vast majority of immigrating buyers who have the means to buy your business are experienced, intelligent, and shrewd businesspeople. They are not going to give you a suitcase full of cash for your business. And with the ability to search and compare businesses online, they have access to the same knowledge and investment options as all domestic buyers.

To summarize, the most likely buyer will be one that has no industry experience, perhaps relocating from outside your area, and will be willing to pay a reasonable market value for your business. But there are many steps beyond finding the right buyer. As we said earlier, it is one thing to get a fish on the line; it is quite another to land it in the boat.

CHAPTER 4

THE WORLD OF FRANCHISING
RAY TITUS, CEO UNITED FRANCHISE GROUP

Ray Titus is the CEO of United Franchise Group, which he built into the global leader for entrepreneurs, with over 1,600 franchises in more than 80 countries.

He is a life-long entrepreneur who began his career with his father, franchising legend Roy Titus. Ray founded the first Signarama store in 1986 and went on to develop a group of successful brands and franchise development services.

Ray's awards and honors include the prestigious "E" Award from the White House, which was given to both Signarama and United Franchise Group, and being named Florida Entrepreneur of the Year by Ernst & Young. He has published several books, including *Laws of Inevitability, Ray's Week, Put a Little JJ in Your Life,* and *You're Not Listening to Me.*

Ray and his family established the Titus Center for Franchising at Palm Beach Atlantic University, the first university center in the U.S. solely dedicated to teaching students the principles of franchising a business.

TRANSWORLD

Before we talk about your incredible success in the franchise world, let's talk about your background and how you got here.

RAY TITUS

I grew up in Oyster Bay, Long Island, and you could say franchising is in my blood. I learned it from my father, Roy Titus, who started Minuteman Press, the printing franchise, in the early 70's. My eighth-grade school paper was "how to start a franchise company."

After college, I came to work with him. Within a year, we founded the sign business. I started the first Signarama store in 1986, when I was 23, started franchising a year later, and we've never looked back.

Eventually we started United Franchise Group, and today we have 10 brands, 1,600 franchisees in 80 countries worldwide. Signarama is still our largest one with almost 800 franchise owners. Transworld joined the family eleven years ago. Transworld has been the perfect partnership, because we know franchising and Andy and his team know business brokerage.

TRANSWORLD

Not everyone follows in their father's footsteps. Not only did you do that, but you also surpassed him in the growth of franchising. Talk about everything you learned from him.

RAY TITUS

My dad was an early pioneer in franchising. He had been in magazine sales, and he started a company called TV Facts, which competed with TV Guide, except you got it for free at the grocery store. It was a franchise, and the local franchisee made money selling advertising within the TV listings. When they printed the magazines, they liked what they saw about the printing industry, and that's what started Minuteman Press. Today my older brother still owns and runs that company, and my younger brother works for him.

I learned so much about franchising from my father, and some key people who worked for him. The other thing that helped me was I had a sports background. I had gone to college on a basketball scholarship. I learned a lot of lessons in sports that I transferred from the basketball court into franchising, such as the work ethic and goal setting. For me, franchising was always a perfect fit. I know how important it is to help people reach their dream of owning their own business.

TRANSWORLD

Talk about how you went from franchising Signarama to United Franchise Group. What went into the decision to go from franchising one brand to becoming a franchising organization and creating new brands?

RAY TITUS

Signarama was our only business for about 12 years, and it was very successful. But we decided we should diversify the organization, so if something happened in the industry or there was a significant change in technology, we'd be protected.

In 2000, we launched our first new brand, EmbroidMe, which is now called Fully Promoted. It does embroidery screen printing and promotional products such as shirts and caps. So, it was similar to Signarama, but it was a different industry. We started the pilot store here in Florida, and then we started franchising, and we did it all ourselves organically.

As it grew, we realized our skillset wasn't just the sign business, or the embroidery business, it was franchising. That was who we were. We bought another company called Billboard Connection and started franchising that. Then we started looking like NASCAR racers, with all these logos of different brands on our chest, and it dawned on me that we needed one name to describe our family of brands. We did the opposite of most businesses. We had the brands first and then we came up with our name.

We have three food brands, John Smith Subs, the Great Greek, and Graze Craze, which is a charcuterie board and grazing box business. We've added Venture X, which is our co-working space brand. Within our consulting division, Transworld is the largest franchise, but we also have other consulting franchise opportunities, one focusing on networking, one that turns people's ideas and businesses into franchises and one exclusively dealing in franchise real estate.

We do everything from helping people reach their dream of owning their own business to helping them run it successfully and building and growing a great business.

It's been a remarkable 35 years for me. I'm really blessed. I'm only 58 years old, so I'm still young for a CEO. My three sons are all in the business with me. So are my three nephews. We're a large organization, but we're still a family-run business. In fact, our franchise owners often tell me they get the best of both worlds. On one side, we're this large franchise organization with the training, the support, the facilities, everything people would want in a franchise company. But on the other side, we're a privately held and family-run business that franchise owners can build relationships with.

Andy Cagnetta and Ray Titus sign Transworld-United Agreement, 2010

TRANSWORLD

The partnership between Transworld and United Franchise Group is a success story on both sides. Talk about the collaboration. Why was it such a good fit? And give us your insights on how United Franchise Group was able to help Transworld grow so much.

RAY TITUS

First, we headquartered Transworld out of our office, because we wanted to be able to utilize the full resources of the United Franchise Group, accounting, legal, and all services that we have here in the building. That was a very good first step.

I was then able to get one of our key employees who was a regional vice president and a salesperson, Bill Luce, to come on board and really take it to another level. At the time, we had a company called FranchiseMart, which was basically a franchise to sell franchises. When the recession hit, we realized we needed to adjust that business. Transworld came along at the perfect time. We shifted FranchiseMart into a Transworld franchise business, and it worked out great.

We were able to improve on the business model every year. We were able to reinvest money back into the system to get more support and more training and more technology. And since the Transworld business model is so strong, it was an easy sell. With Transworld's great history in business brokerage, and our great history in franchising, we play off each other well. We complement each other.

Let me share a story about why this is such a good fit. Two years ago, I ran into two guys who had a tire and rim business. It was very successful, doing around $12 million in sales a year. We were talking about franchising the business. One of them saw Transworld on my business card, and he said, “Transworld did something for us that we'll never forget.”

Years earlier, they had met with a Transworld broker in Fort Lauderdale, to talk about selling their business. At the time, they came up with a price of $600,000. They would have gotten $300,000 each, before taxes and broker’s fees and other costs. But the broker told them, “I don't think you should sell this business right now. I think you should build it up, and then come back to me. This is a good business. You should put more time and effort into building it. Don’t give up now.”

They listened to him and built themselves a great business. They’ve made a lot of money over the years, and when they do sell, they’ll get a lot more.

The point to that story is, sometimes a broker's job is not to sell the business. But it takes the right type of broker to see that. I’m sure that broker has received more referrals from those guys, and more good will for the Transworld brand, than any advertising would do for us. To me, it’s so important to develop relationships and do the right thing by them, even if that means foregoing a commission. Not every broker would do that. It says a lot about Transworld.

TRANSWORLD
Thank you for sharing that. We believe it's very much a relationship-based business. Let's talk about selling businesses. Obviously, most of the franchises you sell are brand new, but you also help franchise owners when it's time to sell an existing franchise. Talk about how you help them.

RAY TITUS
We've been selling both new franchises and resales for 35 years. When you sell any business, you have to prepare it in order to sell it, and the sooner you can start the process, the better. If you have to sell at the last minute, you're never going to get what you should. So, when we sit down with a franchise owner who wants to sell, that's the first thing we talk about.

First of all, the owner needs to understand they can't be the center of everything. They have to have staff. They have to work on their business, not in it. A new owner needs to see that. Then, they have to have the books in good shape. At that point we look at the business itself. Where do we stand with equipment? How's the look of the store? Is it clean? Does it need sprucing up? Just like when you sell a house, a lot of the real hard work is done prior to putting it on the market.

Once you have all that, then you have to come up with a fair price. As you know, there are formulas brokers use, and certain industries dictate certain formulas, whether it's a multiple or profit or a multiple of revenue or something else. We want to look at everything and price it right.

Then we meet leads and prospects and introduce the resale to them. Our process is different than how a business broker would sell an existing business because we sell the brand, the company, and the industry first, and then introduce the opportunity.

We also don’t have to go looking for listings. We sold the franchise in the first place, so they’re going to come to us when they’re ready to sell. Also, as a franchise company, we have a different pool of buyers. They may already be sold on the brand.

You may remember, in the early years, you and I used to say, "Business brokerage and franchising is kind of like the English and the French. It's like you're speaking two different languages." Which is very true. It’s business sales and resales, but it's a different animal. In most of our resales, we use a broker, and we try to use the Transworld brokers in every market, because they're the best ones. Again, your business model is a very good one.

TRANSWORLD
Thank you. You talked about the process of getting a business ready to sell. That applies whether it’s a franchise or a stand-alone business. Something else that crosses over is the matchmaker aspect. Whether you’re a broker or a franchise company, the business owner is selling something they built for many years, and the last thing you want is a prospective buyer coming in and saying, “I really don’t like the look of this place,” or “That’s something I’ll need to change right away.”

RAY TITUS

One difference between what we do with franchise resales and what a business broker does, is once we sell the franchise, we have to live with the new owner. We have to train them, and set them up, and support them. So, we can't have owners that are not going to be cooperative or work together.

We also have to look at the buyer and whether they're a good fit. Do they know anything about the industry? Do they have the experience and skills to succeed in this business? Some require more training than others, some just aren't cut out for that opportunity.

TRANSWORLD

Speaking of training, business schools don't teach franchising as part of the curriculum, even though it's such a big part of the business world. But you're doing something about that.

RAY TITUS

One day my wife and I were talking, and I said, "I want to give something back locally." Our oldest son graduated from Palm Beach Atlantic University, which is attached to our church, Family Church in West Palm Beach. So, I met with the college and told them I wanted to start a franchise school. I didn't realize we were the first ones to ever do this. But we did it. It's known as the Titus Center for Franchising at Palm Beach Atlantic University.

The number one guy on my list to run the school was Dr. John Hayes, who I've known for years. He's run franchise companies, and at the time we were making plans he was the president of a school in Kuwait. I called him to see if he knew of somebody else I should talk to. As it turned out, his wife had passed away and he wanted to move back to the states, and he said this was a position he'd love to take on. We were able to make it happen, and he has done a spectacular job building the Titus Center for Franchising.

We're teaching students how to own their own franchise and start their own business. We're also teaching them how to be successful employees in franchise stores. We now have a board of directors consisting of more than 40 people from the franchising community sharing their experience and wisdom. It's really grown into a special place.

And now we're not alone. Babson College has created one. So have the University of Tennessee and the University of Louisville, and more are coming. Now we're looking to set up a consortium of universities into franchising, to be able to benefit from each other.

By doing this, we're able to be big promoters of franchising. Obviously, we're big fans of franchising. It's a proven model. We're able to help someone reach their dream of owning and running their own business, and give them the support they need, The training, the vendors, the suppliers, recommended pricing, websites, technology, POS system, everything.

This has also been a tremendous opportunity for us to give back to the local community. I've always been a big proponent of our franchise owners doing that, so for me not to do it would be very hypocritical. We urge our franchise owners to do it, and we need to lead by example and do it ourselves.

TRANSWORLD

When you found out that the Titus Center for Franchising was the first of its kind, what did you think? The franchise model is such a big part of the business world and has been for decades.

RAY TITUS

I don't know why franchising hasn't caught on in the educational system in America, or anywhere else for that matter. It represents 40% of retail business in the United States. It's an incredible industry. It generates more taxes, more jobs, than any other industry.

Now we have students that are going to school to get a minor in franchising. They’re getting internships with dozens of franchise companies. The kids that go through that have such a big advantage over everybody else. That’s what we wanted to do, give them an unfair advantage in the marketplace, in addition to understanding franchising.

TRANSWORLD

Obviously COVID has had a huge impact on franchises and the business world as a whole. It’s a different world today than it was in March of 2020. We’re not going to ask you to look into your crystal ball on COVID, but we will ask you to talk about trends you’re seeing when it comes to franchises and selling businesses, and what you see coming down the road.

RAY TITUS
Unfortunately, COVID has led to a lot of people closing businesses, and a lot of people getting laid off. But we've learned from it.

When COVID first hit, for about a week we were looking at this curveball and we didn't really know what was happening. We didn't know how big it was going to be. But by the second week, we said, "Okay, if this is what's happening, what can we do? What can we sell? How can we pivot our brands?"

The key was pivoting each brand, so the franchise owners had ways to get through this and make money. We were able to do that in every one of our brands. We could do that because, A, we have great franchise owners that worked hard during this crazy time, and, B, we were able to share success stories and things that franchise owners were picking up and doing.

Signarama, which had always focused on signs, was suddenly selling sneeze guards and plexiglass dividers. We became one of the largest sellers of sneeze guards. We also did floor graphics that said, "six feet apart," and other things people needed. Fully Promoted, which does promotional products and embroidery, and screen printing began selling safety masks with companies' logos on them. In our food business, we focused on catering and delivery, because we couldn't do dine-in. We had to really figure each one of these things out.

I think this has been a lesson for everyone to make the changes in your business model that you need to make to get through the time that you're in. We did that, and fast. Bear in mind, our largest expenses have been people, travel, and trade shows. There were no trade shows, there was no travel, and we did have to cut some people, but as an organization, by the end of the year, our organization was as profitable as we had been the year before.

Now we’re able to sell franchises over Zoom. We have people that bought food businesses that never tasted the food. We have people that bought franchises that never walked into one of our stores before. It’s been a learning curve, learning how to do it, and how we go through this. Zoom has been around for more than 10 years, and most people never used it. Now we can’t live without it. Half of our Discovery Day tours are on virtual. Last year, 100% of them were. We were able to embrace technology and be able to take the businesses forward.

From a sales standpoint, we have a larger pool of buyers because of the people who have been laid off. We also have a larger pool of people who want to sell their business, because they got through COVID and they’re done. I think we're going to have a boom of franchises and business sales over the next couple years, because we have this COVID fatigue. Some people who built their business over the years and really struggled during the pandemic, may choose not to start all over again, and there are entrepreneurs out there, that are ready for the opportunity, they will step in and build it back up as their own business.

On the other hand, we have franchise owners that did better through COVID and they’re happy. Signarama just set a record for the best royalty month in the history of the company. I was just in Hawaii with our Million Dollar Circle, franchise owners that have done over $1 million in sales. There were 60 of them from across all brands, and in five days, not a single one said anything to me about dealing with COVID. They did talk about the trouble hiring staff and getting product, but not one person mentioned COVID itself. If we had done this a year ago, that would have been the only thing they talked about.

Our brands are selling their products and services. Business is happening. I think that’s a testimony to the franchise owners and the hard work they do every day.

TRANSWORLD
That’s very good. Over these 35 years, you’ve shared a lot of advice. What’s the best advice you’ve given, and, the best advice you’ve ever received?

RAY TITUS
The best advice I’ve ever given was when the recession hit in 2008-09. We had franchise owners who were reeling. I told them, "Go back to basics. Be the number-one salesperson in your store. Stop any complaining, stop anything else, get out and go sell, and get back to basics." That’s what has to happen in those kinds of times.

As for advice I’ve been given, I've been blessed with so much great advice, much of it from my dad. He was here for the grand opening of our headquarters, which is 60,000 square feet, and after walking the entire place, he said, “Ray, you want to know why I love this place? It’s only one floor. You can never get the ivory tower syndrome if you have a single-floor business."

He’s also given me some tough advice. He said, “When you have to go through a layoff, and you come up with the number of people, double it and you’ll be okay. Because the last thing you want to do is come back and do it again.” I’ve had to do layoffs twice in 35 years, and I hated it. But he was right, doing it once is bad enough, having to do it twice is horrible.

Looking ahead, I tell everyone we have to focus on growth. Our business is predicated on building brands. Nobody wants to be a franchise of one. Everybody wants brand awareness, mass purchasing power, cooperative advertising. So, you have to build the brand. We not only have to help franchise owners grow their businesses, but also grow the brand by adding more franchises.

I also want to say, from my standpoint, over 35 years of building and growing brands, our relationship with Transworld is one of the things I’m most proud of. It is one of those opportunities that I consider a once-in-a-lifetime scenario, where everything aligned to make this where we're at today. We’re the largest business brokerage in the world, and the fastest-growing one as well. It’s exciting to see what has happened over the past eleven years, and I’m looking forward to what’s yet to come.

TRANSWORLD

So are we! Thank you for sharing your experience and expertise. This will benefit a lot of people, not just franchise owners.

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CHAPTER 5

DON'T GO IT ALONE

Hire the Right Broker

Who is the right broker to sell your business? In our opinion, it's not always a person who is intimately familiar with your business. Can that insider knowledge help? Sometimes, but is it relevant? We don't think so. Would you hire a heart surgeon just because he knows you personally? No, of course not. Wouldn't you rather have an expert surgeon—one that has done the procedure hundreds, if not thousands of times?

That is what you want in a broker of your business: someone who knows the process and can help coach you through the complicated and often emotional journey. You need and deserve much more than someone that is familiar with your specific business or industry. You want someone that will find the right buyer, at the right price, and get the deal closed!

Finding the right buyer is about casting a very wide net in order to attract that perfect someone or company to buy your business. Getting the right price and terms is having the ability to create competition for your deal. The more buyers you have, the better the price and terms will be.

Additionally, closing a deal without a buyer trying to re-trade during due diligence or even at the closing table can be prevented. It is best discouraged by the threat that there are other buyers waiting in the wings to step in if this one defaults on the deal.

The right broker has the tools to succeed. He or she has a large network of brokers at his/her disposal, and is willing to co-broker with them and split the commission. If your broker will not work with other brokers and share commission, I would consider moving on. Historically about a third of Transworld's deals have multiple brokers. If your broker is the single source of buyer flow, you are hurting your chances for a successful sale at your desired price.

CASE STUDY – NOT CASE CLOSED

We met with a very successful restaurant owner who owned a Japanese/sushi place in Pennsylvania for over 30 years. He hired a friend from his community who was a real estate broker to sell his restaurant and the building it occupied. That broker "secured" a deal in the form of a nonbinding letter of intent (LOI). He did not explain that an LOI really doesn't obligate the person offering to buy the business to close on the transaction. It got bad as the deal progressed. The restaurant owner mistakenly closed his restaurant and went on vacation for a month figuring he had sold his restaurant and building.

CASE STUDY – NOT CASE CLOSED *CONTINUED...*

Near the end of vacation, he got a call saying that the buyer couldn't do the deal after all. He then had a closed restaurant, no employees and a liquor license he wanted to sell and no prospects to get a deal done. And now a huge amount of the value of the business had vanished.

Your potential broker should also demonstrate personal success at closing deals within their network. How do they advertise? Do they spend money on the right portals? Can they work internationally? Do they leverage technology? Do they have a database of buyers? There are many metrics used for being able to properly market and network the sale. Again, less important is the question of "do they know my business?" What is more important is that they know business brokerage.

Lastly, is your broker someone you trust, and that others trust? Is he or she a trusted advisor in your community? Do they give back and give knowledge to others? Are they problem solvers in your community? This is a person with whom you are going to share intimate details of your business and financial affairs. This could be the biggest financial transaction of your life. Get the right person to partner who has the tools to execute and close the deal! Knowing that person is well respected by others in your community is certainly an indication they can be trusted.

Have the Right Team

We often liken selling your business to playing football. The broker is a good quarterback and you're the player wanting to score a touchdown (sell your business). A good broker is going to call plays and leverage you and several others on the team to get in the end zone. The team is comprised of lawyers, accountants, buyer, bankers, landlord, you, and the broker. As quarterback, the broker needs to help you get in the end zone by calling plays, setting strategy, and using the other players to enable the whole team to move forward. When you have a deal, you're in the red zone (right near the goal) and it is essential to work together to get over the goal line.

The broker is the only one in a transaction that can speak with everyone. Lawyers, accountants, sometimes the bankers and others may only speak to their clients and fellow professionals. And when there is bad news or tough questions to ask, you'll want someone else to do it. Therefore, let all the information flow through the "quarterback." If you keep answering the easy questions, you will eventually be obligated to continue to answer even the tough inquiries or negotiate for yourself.

In the end, you must be strong and make decisions based on advice from all your teammates in the deal. Most deals are difficult and will experience challenges along the way to the closing table. Don't lose sight of your ultimate goal, which is to get a deal done. It is easy to be distracted by things that may bruise your ego or small issues that will test your patience.

The Right Attorney

The key player on your team is your attorney. Your brother-in-law who has a general law practice may have done your will or handled your house closing, but he's not the correct choice at this time. You need a specialist who has lots of experience with your size transaction. For most small transactions, an attorney who often works with business brokers is a great choice. If your business has less than $250,000 value, you are probably going to be best off with an independent solo practitioner. They have the ability to work on smaller deals and be flexible with their time and fees.

If you have a higher-valued or complicated transaction with issues like real estate, taxation, intellectual property, employment, federal or local licensing, financing, industry-specific nuances and so on, you may need a firm that has the resources to handle your business sale. The fees will be higher but selling your business correctly with the right protections and paperwork written by a capable firm is a very smart investment.

You need a "deal maker" who is calm, intelligent, and has sold small businesses in the past. Also, you and your broker need to drive the sale process, as attorneys and CPAs are risk averse. If they advise you to move forward and sell or buy, there is a potential downside for them. If you are selling, they may be losing a customer and revenue. If you are a buyer, they run the risk of you not doing well and holding them accountable. The best scenario they can hope for is your status quo: not selling or buying. Therefore, take their advice on legal issues, realizing that entrepreneurial risk will rarely be their choice of counsel. It is incumbent upon you to drive the process. You need to be the boss.

CASE STUDY – GETTING INDIGESTION

We had a really nice business for sale, a two-location hamburger fast food business that had been around for almost 50 years and was a local favorite. A buyer came in before it even hit the market and had the inside track as he was friends with several members of the ownership group. His price was accepted, and he was ready to close. Unfortunately, his choice of counsel was misguided. The extremely large and overreaching contract, with many warranties to be assumed by the seller, scared the ownership group enough to call us to find another buyer. We were quickly able to find other buyers that agreed to pay more money and buy with a standard agreement with reasonable terms. It was a huge lost opportunity for the original buyer.

CHAPTER 6

LEGAL MATTERS

DEBORAH CARMAN, CARMAN LAW FIRM

Deborah A. Carman is the founder of the Carman Law Firm, P.A. in Boca Raton, FL. She has nearly 40 years of experience practicing law in Florida, and her firm has a long history of successfully closing real estate and business transactions. Prior to starting her own firm, Deborah was house counsel for a major insurance company.

She is also the owner and President of Palm Title Services, Inc., a full-service title company serving Florida for more than 25 years.

Deborah is a past president of the Broward County Woman Lawyers Association, has served on numerous boards, and regularly teaches contracts classes for the Palm Beach County Board of Realtors.

TRANSWORLD

You're an accomplished business attorney in Boca Raton, Florida. How did you get to this point in your life and your career?

DEBORAH CARMAN

I was born in Philadelphia, but we moved to North Miami when I was only three months old, and that's where I grew up. After graduating from North Miami High I went to Tulane University in New Orleans, and stayed there for law school.

Growing up, my father was a builder, and he was the old-fashioned type, which meant if he shook your hand, he would do what he said and what he needed to do. We don't have much of that anymore. Ironically, all three of his children became attorneys. My two brothers and I all practice law here in South Florida.

TRANSWORLD

You didn't always have your own firm. Talk about how you got started in your law career and what led you to start your firm in Boca.

DEBORAH CARMAN

It's interesting, I actually started out doing maritime law. That's one of the things Tulane is known for, as well as oil and gas. When I graduated in 1983, oil and gas was no longer a desirable field. There weren't many jobs. That was also the case in maritime, but I had secured one. However that firm disbanded a year later. I worked for Aetna for a while, then decided I wanted to open my own firm.

When an attorney starts their own firm, they do just about everything. That made it a very interesting learning experience for me, because when you do everything, you can see how everything fits together.

TRANSWORLD
At what point did business law become your focus? What led to that decision?

DEBORAH CARMAN
I enjoyed being able to do all different types of law, but I found that I enjoyed business law the best. I still do real estate, both commercial and residential, but I have a title company for that. For me, business is it. There are a lot of moving parts in businesses.

It's kind of funny because as I mentioned, I started out in maritime, and I love contract law because I started doing that with someone who was building boats. I cut my teeth on boat-building contracts and merging them with bigger companies. It was a lot of fun and I said, "This is what I want to do."

TRANSWORLD
And you’re doing it very well. Talk about your role in the process of making a deal happen.

DEBORAH CARMAN
My role really is to be part of a team. Sometimes I serve as the quarterback on that team because I look to see what the seller and buyer need to do in the transaction. Sometimes I'm

a facilitator, and sometimes I'm just giving advice. It all depends on what it is and who is on the other side, because one of the things I love to do is work well with the other attorneys, whether I'm doing buyer side or seller side. If a buyer wants to buy and a seller wants to sell, we get the deal done. I want to make sure we get it done in a way that's going to take care of the clients, but also get it done so they have that part behind them and move on.

What's so interesting when you work with sellers is this is their baby. They've taken a long time to build their business. There's a lot of pride there. You have to give them proper respect for building that business. I think that's why a lot of attorneys don't understand business and one of the reasons I enjoy this so much. I love business. I live it with my husband, who does lending. So we sit there and eat, drink and breathe business, and when you do that, you really come up with close contact with your sellers and your buyers.

TRANSWORLD

Let's follow up on something you said. When someone is selling a business, "This is their baby." Very often it's someone who started a business and ran it for decades. It supported their family. Now they're selling it. And they have a big emotional attachment. It's like someone selling the house where their kids grew up. Realtors will tell you their biggest challenge is to get a homeowner to step back from that emotional attachment. How do you talk to your clients about that, and get them to realize this is a business transaction?

DEBORAH CARMAN
That's a great question. What you do at Transworld is find the best fit for that buyer and seller. Once you have a good fit, it's easy for me then to get this to move forward. When you have a bad fit, I know almost instantly. The two sides are fighting. I tell my clients, "Never fight with the other side, let your attorney do it. You want to blame something on me? I have very broad shoulders." One of the things we look to do is separate that emotion from the buyer and the seller and make it really a pleasurable event for them. We want the seller to see how the buyer is going to take the business forward. Maybe some capital is going to be infused. Maybe there's going to be an additional marketing. Make it a positive situation for a seller so he can actually see where his business is going to wind up.

The worst thing to do is have a seller come in that's emotionally attached, and have a buyer that immediately wants to change everything about that business, or the buyer calls the baby ugly. When you have a situation like that, emotion takes it right off the charts. Once you've taken a personal stand, it's very difficult to come back from that. I always tell buyers and sellers, "This is not personal."

I was a psych major, so I try to put myself in their situations. I also had a very good mentor to teach me about energy, so I can actually read the energy for the people, understand where they need to go. In addition, I always try to remain calm. I think out of all the gifts I have, the ability to remain calm is what really allows me to get these transactions done when there are challenges. I can remain calm, and hopefully everybody else calms down. Not to mention, we usually have chocolate chip cookies at our closings, which sounds silly, but actually calms people down.

TRANSWORLD

Chocolate chip cookies are good for a lot of things. In addition to the emotional attachment, what are some of the other common challenges you help business owners deal with during this time?

DEBORAH CARMAN

I try to make sure people tell me what skeletons are in their closet ahead of time so I can help them. People don't always understand that as their attorney, I keep what the seller tells me confidential. So if you have an issue, let me get it resolved for you instead of letting it fester and have it come out at the very end when we're ready to close. Now I can't get the closing done for a period of time and it leaves a bad taste for everyone. I want to know everything that could possibly happen up front so I can get it resolved.

I have to tell sellers, "If you have problems with your employees, or your lease, or your partners, you need to let me know now so we can get them resolved and get this deal to occur." Or if they're underwater. There are a lot of people who are in that situation, particularly as we've gone through COVID. They may want to sell, but they won't get enough money to pay the debt. I need to know that early on.

TRANSWORLD

You don't want any surprises. You need to be prepared. The last thing in the world you want, or they want, is to have something come up at the end and have the deal blow up in their face.

DEBORAH CARMAN

Exactly. What's nice is when I work with an excellent business broker and I work with the CPA and I work with a lender, we're a team. Whether I represent a buyer or a seller, it's nice to have that team together, because we can smooth things out. We can talk to each other. There are so many things I can get done. Remember, I'm dealing with another attorney, who has to go back to their client and deal with all the emotions and everything else. It's much better for me to have someone who can go ahead and facilitate the deal for me and make things happen and understand what's going on. Now it all gets done for the client and it works out perfectly.

TRANSWORLD

Having that team is an important component. Business owners may realize they need a business broker to help them sell their business, but they may not be thinking, "I also need a good attorney, and a good CPA, and I may need my financial advisor involved in this." Not thinking about that team concept is a big mistake.

Another common mistake we see is business owners taking their pedal off the metal once they decide they're going to be selling in a few years. If they begin coasting instead of constantly thinking about growing the business, when the day comes that they're ready to sell, the business may be worth less than it was several years earlier. Can you talk about other mistakes you’ve seen business owners make as they lead up to selling their business?

DEBORAH CARMAN

A lot of mistakes come about because they don't understand their financial situation or the legal situation they're in. They don't realize that if there's a lawsuit against their company, they have to resolve it before they can sell. Then there’s the issue of partnerships. Some owners go ahead with selling without making sure their partner is on board with the plan. Sometimes an owner and their spouse are divorcing. What do we do with the business in that case? There are a lot of different issues that can come up, and again, emotions can play a role.

You have to go through every single scenario and make sure you put yourself in a good position. Whether you owe money to the IRS or anyone else, whether you have an issue with your liquor license, all these things have to be brought out and looked at before you go to sell the business. A lot of times you have a seller that's just tired. They've worked hard for a lot of years. Then something like COVID happens, or the economy changes, or other issues surface, and they don’t know what to do with this business they’ve built up for 25, 30 years. That’s where I come in. This is where I try to be the quarterback I referenced earlier.

There are so many things I learn on a regular basis every day about what someone's doing with their business. As an attorney, you have to immerse yourself in their business because if I don't understand their business, I'm going to miss something to help me tell them what to do and where to go. Sometimes that means telling them it will be a few years before they can sell, because that's how long it will take to work through the issues. This is where having that team is so important.

TRANSWORLD

You mentioned partners. How many businesses do you see where the partners never did a buy-sell agreement or a succession plan, something that would protect them down the road?

DEBORAH CARMAN

I'd say a good 75% of the businesses with partners do not have proper buy-sell documents. A lot of them started out on a handshake, or one provided the financing and the other provided the sweat equity, and all of a sudden you have unhappy people because they can't come to a decision about how to break up the pie. When you're starting out the honeymoon phase always looks good, but you always have to plan for the exit strategy. Not just for when you sell a business. What if one partner has to leave? What if there's a divorce or a death? If people don't take the time to plan properly early on, there can be a real problem at the end.

TRANSWORLD

There are a lot of steps business owners need to take over the course of the lifespan of the business. Certain things early on, certain things as you grow, certain things as you approach the exit. What are those steps when it comes to the legal side of things?

DEBORAH CARMAN
When you start your business, you want to make sure you have the proper shareholder agreements, proper operating agreements and so on. Have everything done professionally so if there is a divorce or a death or anything comes up, you're going to have someone to take care of the business.

This is where you get a good CPA on board. I always defer to CPAs as far as taxation questions. You want to make sure you have that person on board so you’re not going to do something that will come back and bite you later.

Then as you build the business, make sure you have proper contracts, because no matter how friendly you are with a vendor or supplier or customer, no matter how many dinners you have or football games you go to, you have to be able to sell when it’s time.

Probably the hardest thing for a small business, especially a service business, is it’s the person. So how does the person take that and make it something sellable when you’re the one that’s provided the service? That’s where contracts come in. Make sure there’s assignability for those contracts. That can include employees. Maybe you should have a non-compete clause with your employees, to keep them from going to a competitor. Contracts are so important.

The internet has probably hurt our business more than anything else because everybody's a lawyer. All you have to do is go online, get a form and fill it out. Now you’ve done your own will, your own contracts, everything with your company. But no one has looked at it and blessed it. That’s really what it takes. It takes people to look at what you've done and make sure you can continue to grow. Make sure you have a strategy, not just for exit, but a strategy for growth. As attorneys, we look at every part of the contracts. We look at everything you've done in your business to make sure you have those strategies in place and put you with the appropriate people.

TRANSWORLD

Often in a small business, the owner is wearing multiple hats. They’re the CEO, the sales manager, and so on. That’s certainly something the buyer needs to look at. You mentioned contracts with vendors. What if most of their supplies come from one vendor, or 80% of their revenue comes from one client? What about the employees? Will the key employees stay on after a sale? Those are all things that can impact a sale. Talk about that from the buyer's perspective.

DEBORAH CARMAN

When you look at everything from the buyer's perspective, customer concentration is a real issue, particularly when it involves lending from the SBA, because that's one of the key components. They don't want you to have just one customer. They want you to be diversified in case something happens and that customer leaves. Even with SBA lending, sometimes there’s a seller note, and if there’s no SBA lending, there’s usually a seller note. So how do we protect the buyer? Do we have earnouts over here? If there are five customers and one leaves, is there a way to offset that business note? Is there a way to do something to protect the buyer?

Is the seller going to have a contract with the buyer, consulting agreements, independent contractors agreements, employment agreements? What is the situation going to look like so the seller and buyer could continue to work together to build this company? Maybe what the seller needs is a job. That's something else for the buyer to look at. What is the seller looking to accomplish when he sells? Is the buyer going to be able to grow this business or is this business totally oriented around the seller? Sometimes we'll do a stock purchase, and bring the buyer in for a period as a partner. There are ways to keep sellers on in the purview of the public so we can transition in the buyer.

This comes back to what I said earlier about it having to be a good fit. If you have a seller that is really bubbly and very enthusiastic about it, and a buyer that literally just wants to sit there at his desk, it's not going to happen with those same customers. So you have to see what that mix is. I remember when IBM had all the layoffs and gave out severance packages, I had a client who took the money and went into a packaging business. It was not the right business for him. About a month later he called me and said, "I hate this business. I don't want to be here. I don't want to do this." You have to make sure it's a good fit. That's where a good business broker comes in to play. They make that good fit happen. They see it, "These people can have a synergy."

TRANSWORLD

The business broker has to be a good matchmaker.

DEBORAH CARMAN

Yes, because it has to be a good match. I can light that fuse and keep it going, I can get it close, but if it's not a good match, it makes it 10 times harder.

TRANSWORLD

Is there a difference from your perspective if someone is a franchise owner versus a standalone business?

DEBORAH CARMAN

With the franchise, you know there were royalties paid so it's a little easier to get a handle on the financials. It's a little easier to understand what needs to be done. Someone doesn't have to recreate a business. There are steps in place for the seller and buyer to follow. So in that respect, they have a support system, and if it's a good franchise, that support system will carry them forward. You also have another level of training and everything else that has to be done to qualify that buyer. So to some extent, that buyer's going to have to be a better fit, because otherwise they're not going to like what they're doing. On the other hand, you've also introduced another party, which means you'll need a consent from that party as well.

TRANSWORLD

In some ways, it helps because there are more things laid out that you already know are there. On the other hand, there's that other layer of complication.

DEBORAH CARMAN

Most people, by the way, don't understand how to read the FDD. They don't understand what everything is with a franchise and it gets them hurt down the road if they don't understand what they're buying into and what's going to happen if they want to terminate the franchise. People who think because they’re buying a franchise they don’t need a lawyer are very wrong.

TRANSWORLD

You talked briefly about COVID earlier. How has that impacted things, and what trends are you seeing now?

DEBORAH CARMAN

When COVID first happened, I was very nervous because business stopped. Literally everything stopped. Real estate stopped, business stopped, everything took a turn and we said, "What's going to happen over here?" It wound up being a really interesting situation. I believe more businesses have been sold during COVID than any other time, because where else can you get a buyer that already has an existing model, can take that and go with it, and doesn't have to do a startup? In that respect, you save that impact. A smart seller made a deal right away with the landlord to get rent deferred. Business owners got paycheck protection program loans and other assistance from the government.

People got very smart. Sellers looked at how they could protect their businesses. Now that created challenges because you have to get rid of them when you sell the business. All kinds of permission, consents, rules, regulations apply. But it still winds up being a good situation because a buyer has a much healthier business when they take it over.

There were a lot of changes. The biggest is, “How much do I pay?” This business was doing great. All of a sudden it tanked. What does that mean? Does that mean the next year it's going to do well again? Will it ever do well again? How has COVID affected it? So earnouts have become very popular, and that's how people tend to value the business. "Okay, you say XYZ was done before. Well, if XYZ can be done again, let's continue this talk and let's get this done, but we're going to do an earnout and make you show that this business will succeed." So in that respect, a lot of changes were there.

TRANSWORLD
Where do you see things a year, two years, five years from now? Buyer's market, seller's market, growth market? Where do you see all of this?

DEBORAH CARMAN
What I'm seeing is that it's a weird situation. It's not like real estate. Real estate is clearly a seller’s market right now. But for business, it's always going to be the same in the sense that people don't want to open a new business, they like to build upon what a seller has done, and those will last for a long period of time.

Even now, I’m seeing restaurants, bars, different things that were impacted by COVID are coming back. Small business, which is the mainstay of our country, will always continue to be coming forward. I don’t think it’s going to be either a buyer’s market or a seller’s market, it’s going to be a situation of what you want to do and finding that right fit.

TRANSWORLD
What’s the best advice you’ve ever given in this area?

DEBORAH CARMAN
It’s what we discussed earlier. Take the emotions out of it. Do what you really need to do. For a buyer, make sure you do financial due diligence. For a seller, get everything organized ahead of time. Before you look to sell the business, make sure all your ducks are in a row so there are no last minute surprises. Buyer or seller, the best advice I can give a client is to make sure they know what they're doing.

TRANSWORLD
That’s excellent advice. Thank you for that, along with all the other insights you shared.

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CHAPTER 7

GETTING IT READY

Getting a business sold will include the due diligence period where a buyer will review all the information to verify the business value, performance, and representations that you made to effectuate the offer that is on the table. We often call due diligence “show time,” because your ability to verify the representations made during the showings, discussions and in the offering memorandums (or listing information) will make or break a deal. With this in mind, making sure your financial house is in order is a top priority from the day you decide to sell.

Get Your Books and Records Up to Date and Organized

This means gathering all your past tax returns, payroll tax returns, bank statements, QuickBooks files, leases, loan documents, equipment purchase documents, etc., and getting them digitally scanned and organized into some single file or virtual deal room. If due diligence is done in person, you must have all the printouts organized and ready to lay out in a deal room.

If a buyer’s accountant walks into an organized room or logs into a virtual deal room and can find all the files properly named and categorized, this reflects the business' organizational structure and overall quality.

CASE STUDY – NOT SO HEALTHY

We had a nutrition-health store listed in a prime location. The seller procrastinated over getting us the financials. When a buyer came by to look, they insisted the seller provide recent financials. He dug under the counter and produced a few notebooks and shoeboxes with loose receipts. That alone would have killed the deal. But making it even worse, when we toured the building, it was discovered he (and his cat) were living in the back room! There was a big screen TV, couch, mini-fridge, microwave, and clothes scattered about. Needless to say, the buyers politely excused themselves and didn't make an offer.

The key to success in this critical juncture is to have the findings in due diligence match exactly to the representations made in any offering memorandum or listing package provided to them earlier. When buyers run into inconsistencies in the financial information everything is then suspect. As we like to say, the seeds of inconsistency grow wildly once planted in a buyer's mind.

Several years ago, we got a call from a man who had bought a pool business for his son. The son hadn't done a good job of running the business, so there were very little profits on the books. Consequently, it never sold. The father was forced to close the business and he lost everything.

If your books and records are not due diligence ready, then you need to take corrective action immediately. If you do not have a CPA that can handle cleaning up your books and records, you need to get a new one or hire a firm to help run the project. The same goes for having time to help in due diligence. Accounting firms are usually busy from November through April. Getting them to help you during this time may be a tall order, so consider timing when planning your organizational strategy.

Keep perfect books and records from now on

We could write an entire book about the myriad of ways business owners have hidden income as a tax savings strategy. But let's just say, in terms of hiding income, the lesser of two evils is over-expensing things like autos, travel, meals, etc. on tax returns. We can usually identify and adjust discretionary expenses and show a buyer the value of that re-casted income.

The worst evil is when revenues are hidden from the financials through other "cash" earned by the business. The classic example is businesses that have some cash transactions that are never deposited in the bank. These past profits are often hard to recast unless some "off book" ledgers are kept.

If either tax savings tactic, grossly over-expensing or under-reporting of cash, is being implemented in your business, it must end immediately. If a typical business sale process is nine months, then a near-term improvement in the profits can translate to immediate increase in value. Remember, if small businesses sell for two or three-times earnings, every dollar of new profit can be two or three at the closing table.

CASE STUDY – EASY AS PIE

A pizza restaurant we sold is an excellent example of a seller who started keeping good books and recovered value. The business originally showed an SDE of $60,236 when we met and they wanted to exit within the next two years. We convinced the business owner to put everything on the books and in the following year his SDE jumped to $153,380. It subsequently grew to $163,353. We were then able to base the price on the strength of the two strong years of SDE to obtain a lender pre-qualification on the business which greatly enhanced its salability. A buyer was located and the eventual sale price reflected the increase in SDE and the ability for the buyer to leverage their purchase with an SBA 7A loan. The business sold for $350,000!

Having bad books in the past will hurt your value, but at least having six to nine months of great books is better than nothing. It could be the difference between selling and never selling your business.

Read your Lease

It is very important for you and your advisors to have a strategy as to your business location's lease assignment terms. If location is not important to your business, this will not be an issue, but if it is, a plan of how to get a lease assigned could be essential to both the value of your business and the ability to ultimately sell.

A buyer is going to want to have the ability to not only keep your location for long enough to make his or her money back (return on investment) but to profit well in the future. If there is bank financing involved, there will have to be a lease long enough for the business to stay through the term of the financing. SBA 7A type loans usually have a 10-year term.

Most assignment clauses in leases will require the buyer to be "approved" by the landlord. This is where having a business plan or great buyer profile and application could make or break a deal. Most landlords will require you to stay on the lease through the balance of the term. If you have a personal guarantee, you will have to stay on the lease behind the new buyer.

If you have a long-term lease in place, with favorable pricing terms, this could increase the value of your business. If you do not have a lease, or are month-to-month, and you're in a place where lease rates have appreciated greatly, a new lease with large increases could lower the value of your business. It could even keep your business from selling.

So, if you have less than a couple years left on your lease, with no options to renew, should you renegotiate now or leave it to a buyer? The answer depends on whether you think you can get better terms for a long-term lease than a new buyer could. But that is rarely the case. Landlords usually see new ownership as riskier than an established owner. Therefore, they will raise the price, and that will hurt your business value, unless you can in turn raise your revenues.

We often advise our sellers to continue to run their business in the same manner they would if they were not going to sell. Since having a solid lease in a business that is reliant on the location is clearly imperative, it would be wise to have time on your lease through the term and options to renew.

There are other issues that come up in a lease assignment. If your buyer has bad credit or is an immigrant and has no credit, landlords can deny the application outright, demand you stay on the lease personally, or even ask for huge deposits. We have seen them ask for one year of rent or more in deposits. If the buyer is using most of his or her available cash to purchase your business, the sale could be in jeopardy.

We have also seen some crazy clauses in leases. In one case, we were told that a simple request for an assignment of lease would be grounds for immediate termination. Therefore, even asking for an assignment could get you evicted. Another beauty we’ve seen is that if the assets or goodwill of the business are sold for above original value, the rest of the proceeds go to the landlord. Therefore, all the proceeds of the sale could go to your landlord. These are unusual scenarios, but important to be aware of before we start the sale process. These are all reasons to meet and negotiate with a landlord up front.

CHAPTER 8

REAL ESTATE, REAL CHALLENGES

ALAN KAYE

Alan Kaye is the Managing Director for Transworld Commercial Real Estate. His commercial real estate experience includes multi-family, land, development, mixed-use, retail, industrial, office, hotels, tenant representation, landlord representation, due diligence and consulting, resulting in over $1 billion in commercial real estate transactions.

Previously he was the first Florida broker to join Marcus & Millichap's venture into the Florida market, served as Managing Director for Coldwell Banker Commercial Southeast Florida overseeing 100 brokers, and was Commercial Managing Director for Douglas Elliman.

Alan is also a former practicing attorney in Florida and New York, specializing in business transactions and real estate.

TRANSWORLD

Let's begin with a little about your background. How did you get started in life and in business?

ALAN KAYE

I grew up on the south shore of Long Island, in Lido Beach. Unlike today when we like to know where our kids are most of the time, back then I would take off on my bike after school to play ball and my parents wouldn't see me until dinner time. There was never a worry or a question whether I was okay. Life was easy and carefree back then. It was truly a great place to grow up.

I started working in residential real estate, in our family business when I was 18. Unfortunately, my father passed away from a heart attack when I was 19, so I had to take over the business. After a few years, I realized if I wanted to improve my game and my career, I'd better go to law school. So, I attended Hofstra School of Law while still working, which actually was a great experience because it gave me more of a sense of discipline.

When I was working, I knew I had to focus on selling homes. When I had my study time, I knew I had to focus on the books. This work ethic has helped me throughout my career, both in law related matters and in commercial real estate.

I moved to Florida in 1992 full-time and in 1996 I was approached by a national real estate firm called Marcus & Millichap. They were based in California, and opening their first office in the state of Florida. I thought it was a good opportunity, and transitioned over to commercial real estate, the same night I met my wife-to-be.

From being a top producer at Marcus & Millichap, to joining other real estate firms and learning what to do and what not to do, I went on to a position as managing director for Coldwell Banker Commercial for nine years, overseeing over 70 commercial brokers and mentoring many others in the business. A friend was an executive at Douglas Elliman in Florida, and I later joined that firm because they also said they wanted to grow their commercial business. While I was there, I joined a networking group, and happened to meet a business broker from Transworld Business Advisors named Randy Bring. We became friends, and began referring clients to each other. We both respected each other's professionalism. Then one day he asked me if I would consider joining Transworld. So here I am. As you know I'm heading up the Transworld commercial division for Florida, and it's fabulous for me. I'm back with people who understand doing big deals, sophisticated business deals and finance.

Residential is an emotional business. Commercial is a logical business. "What's my return? How will this benefit me? Will it be a good building for my business? Will I be able to take it and grow the value?" It’s what we refer to as value add, and it’s something I’ve always enjoyed. When I practiced law, I was a real estate and transactional lawyer. I love the aspect of being able to visualize a project, actually bringing it to fruition, and then having a conclusion and moving on to another matter.

TRANSWORLD

You have quite a well-rounded background. You’ve done law, you’ve done residential and commercial real estate, and you’ve worked directly with a variety of clients. Let’s talk about business owners and commercial real estate. What are some of the common challenges business owners face when it comes to the real estate end of their business?

ALAN KAYE

Historically, if you owned a business and a building and you went to a commercial broker, the commercial broker would push the value of the building. If you went to a business broker, the business broker would push the value of the business. One of the things that attracted me to Transworld was that we have the expertise to maximize value of both for our clients.

Case in point, we just closed a high-profile transaction with The MAI KAI. It’s an iconic business in Ft. Lauderdale that’s been around for 65 years with the same family. The land they own has appreciated at a greater rate than the business. So, while there’s substantial value in the business, there’s more in the land. That’s happened multiple times. We do deals like this all the time.

TRANSWORLD

Let’s talk about the “buy versus rent” decision. When someone has a business and they look at, "Do I buy a building? Do I rent an office? What do I do here?" Talk about the thought process that goes into that decision.

ALAN KAYE

That's a fabulous question. Not just because I'm in the commercial real estate industry, but I've always been an investor as well as a broker. I strongly believe in owning real estate. I believe in the power of real estate, the appreciation of real estate, and the tax deductions of real estate. Historically, if you ask a lot of people in our industry, a business with real estate is worth more money, because you control your own destiny, as opposed to going to a landlord. If you are selling your business and your landlord will not renew your lease or give you a new lease, that negatively affects the value of the business. If you have your own real estate, you control your own destiny. If you don’t need anyone's approval, that ultimately increases the value.

I'm a big proponent of owning real estate. I believe in building equity. If you look at what's happened in places like South Florida, the real estate has appreciated at a much greater rate and a much greater value than the majority of the businesses.

That being said, you have to be sensitive to market conditions. Don't overpay for the real estate. Make sure you're getting a good value. Also, see what your long-term strategy is. Some businesses lend themselves more to being moved to another location. Others thrive based on their current location, where people know them, and moving someplace else would cause them to take a step back in their business before they could move it forward.

TRANSWORLD

Let’s talk a little more about location and being near a competitor. We know that if there’s a McDonald’s somewhere, there’s going to be a Burger King nearby.

ALAN KAYE

CVS or Walgreens will purposely go into a location in South Florida where there already is a competitor, because they want to cut into that market share. Fast food franchises do it because if one drive-thru is busy people might choose a different one. Or they think, “I had McDonald's yesterday. There's a Burger King or Taco Bell, I’m going to try that." There's no question that being together helps.

A different example of strategy when it comes to close proximity is Publix, the predominant supermarket in South Florida. They will put stores close to one another because they want to monopolize the market. You’d be surprised to see the stores so close together, but they’d rather be there than have another chain come in.

In addition to location, visibility is crucial. Even though Publix is set further back in the shopping center, they make sure they get monument signage up front so people can see that as they drive by.

Obviously, businesses like fast-food restaurants want to be on a street with high traffic. Access is also important. Is it easy to turn in? Is there a signal light in front of their location or their plaza? Can you make a U-turn if you’re on the other side of the street? For instance, Dunkin Donuts may want to be on the side of the street where the heavier traffic is heading toward work in the morning, rather than coming back in the afternoon. Location is number one, then demand.

TRANSWORLD

Let's look at how real estate impacts a business owner as they approach their exit. If someone is thinking they're going to sell their business in three to five years, what should they be thinking about pertaining to real estate, whether they own or rent?

ALAN KAYE

If they're renting, the best piece of advice I can give to a tenant is to stay on excellent terms with your landlord, right from the beginning. Don't have any issues. Because some landlords have a very long memory, and when it comes time to renew your lease, they will use the opportunity to get retribution. Unless there's an egregious error or fault by the landlord, always try your best to keep a good relationship.

In terms of ownership, I would make sure I keep up with deferred maintenance on a regular basis. And I would stage my building before I sell my business. I would make sure it looks great. Yesterday I walked a property with an owner who's very hands-on, and he noticed there was some mold on the walkway from the sprinklers. If it's not already gone, I guarantee it will be within days. It's important to maintain the reputation that your property is always in excellent condition. Then before you go to sell, I would go through and take an objective look. Does it need to be painted? Does the roof need to be cleaned? Do you need to refresh the landscape?

How does it look when somebody walks in? What's the sense of arrival like? Because you want to make it look as inviting as possible. That's a real key to getting additional value for your business, because buyers will look for any excuse to reduce their price. From the time we go to contract, my job is trying to make sure that they pay whatever price they agreed to pay, and not try to nickel and dime the seller and reduce it along the way.

TRANSWORLD

When someone sells their house after paying off their mortgage, they get all the money. Some business owners have paid off the loan on their property, others are still paying it off. Talk about the difference for a seller whose building is paid off, versus one who’s still paying the loan.

ALAN KAYE

It gives you more flexibility. For instance, if your building is paid off, you could decide to become the bank, and offer some financing to the purchaser. If you’re the bank, it will defer your gain over time and give you additional income. Plus, you have the benefits of having built up your principal over time, along with potential appreciation.

TRANSWORLD

When someone owns a business along with the building or the land, are they usually owned separately or are they all under one umbrella?

ALAN KAYE

That’s a great question, because as you know what we have to do in every transaction is make sure the ownership is correct. The seller could have a company called John Smith International, but he may not own everything under that name. The building might be owned under the Smith Family Fund. You have to check both entities to be sure. Unfortunately, some people in our business don't check, which can lead to litigation or even heartbreak when the deal falls through. A little preparation up front allows you a more secure transaction down the road.

TRANSWORLD

You have to do your homework. Let’s talk about the common challenges a business owner deals with when they're getting ready to sell.

ALAN KAYE

The first thing is confidentiality. Are they going to lose all of their people? How are they going to sell the business? If they put it out on the open market, are people going to know? Are they going to lose key employees? Second, sometimes when the public finds out someone is selling, they lose confidence and stop going to that business. Those are the primary things on the business side.

On the building side, as long as you're keeping current with your mortgage and your payments, there shouldn't be any implication there. But splitting the business and the building can be a challenge. In fact, we're currently selling a building because the business is being sold, but it’s not going to remain in that location. So, the building needs to be a match for another business, whose owner wants to buy instead of rent.

TRANSWORLD
What are common questions you get asked, and what are the questions that they never ask but you wish they would?

ALAN KAYE
The most common question is “What did the owner pay for that building?" To which I have to say to them, "I'll look it up and I'll tell you exactly, but what they paid for that building has no value as to what the value of the building is today. There's no connection." That’s usually the first thing. Then they start to question, "Is the income you're deriving from the building sustainable? Has the income been pumped up? Can I get the same income if this tenant leaves? How long is the lease? How secure is the tenant? Do I have a personal guarantee? Does the tenant have other locations? What's the tenant's financial situation? How long have they been in business?"

All those questions come up, because sometimes when you're buying real estate, you're buying the existing tenants. You want to know how long the leases are. You want to know if there are any increases over time, even if there’s a Walgreens, which is a Triple-A rated tenant. You start to think, "Okay, this building looks great, but what happens in 15 or 20 years if Walgreens goes out? What can I do with that building? How can I reposition it?" Some people look at the negatives, and other people look at the positives. You might be able to look at the property and know, “It's a dynamic area.

There's high disposable income. There are a lot of people within a five-mile radius. I believe that if Walgreens does go out, I'll be able to reposition the building as something else."

TRANSWORLD

You raised a good point there. For some people, their business is owning property. We've been talking about business owners who also own their building. You also deal with people whose business is owning that property. Talk about their challenges.

ALAN KAYE

You need to see the level of sophistication. Is this the buyer's first deal? Have they done this multiple times? That will determine how they conduct themselves, the questions they ask, and how they proceed. I always like to ask them to tell me about the last property they bought and how it's working out. I want to get an idea of how they bought it, what attracted them to it, any challenges they've had, what they've done to overcome those challenges. I want to find out a little bit about them. That's the best way to judge somebody, because people in our industry have a way of telling you about every deal they were successful in, but they never mention the deals that weren't successful.

I want to know if the owner self-manages properties or has a management company. How does he handle repairs? How does he deal with the tenants? These are all things we need to know in determining what the buyer is looking for.

Many times, people don't necessarily know what they want to purchase. You have to read between the lines. Listen to what's said, but also what's not said, to understand what their objectives are, what they plan to do and how they will perform. Until you close with somebody the first time, you really don't know. They're going to tell you all sorts of things. They're going to tell you, "I'm going to do this. I'm going to do that," but you really have to go through it to see exactly what it's like, and then determine, "Did they do what they say they're going to do?" Unfortunately, in our industry, the ones who do what they say they're going to do are the minority. Often people tell you they have financing but when you ask for proof of funds it turns out they’re trying to tie up properties and find their investors later on.

You learn things over time. If somebody hesitates with proof of funds, it tells you one thing. If they bring somebody else's proof of funds, it tells you something else. You really have to qualify everyone, because when you’re selling businesses and commercial real estate, time is our most important commodity and we need to protect it as much as possible. We need to qualify the people we're doing business with. That doesn't mean you don't take a chance with somebody new if you feel strongly about it, but you need to be able to decide if this is someone you should be working with and investing your time.

TRANSWORLD

As we’re talking today, we've been through a year and a half of COVID. How has this affected what you do, and what trends do you see going forward, not just with COVID, but overall trends?

ALAN KAYE

COVID has had a huge effect, and unfortunately, for some people it will continue over time. Thankfully, I decided to be as proactive as possible and not let anything get in my way. I used it as an opportunity to reach out to everyone I've ever done business with, everyone I could think of touching base with or reconnecting with. For me, it’s actually been a very positive time. I made a list of clients I was working with to determine who I thought would be negatively affected and who was going to ride it out. For some people, it's going to have a long-term effect. Some will be able to bounce back, others won’t. I think it’s really taught us that you need to keep working your business plan. You need to keep moving forward without looking at what other people are doing, without getting stuck.

As you know, in our industry you do a lot of prospecting. Short-term, intermediate, long-term prospecting. Then you get an assignment and you’re working on a property, and your prospecting goes down. The key in our industry is keeping up the prospecting while working on new matters.

You may remember the old juggling acts where they would spin plates on sticks. In our industry, now, not only do we have to keep the plates going, but we have to constantly add more sticks with new plates. That’s why prospecting is key. A lot of people looked at COVID and thought, "This is horrible.”

I stayed positive, and it positioned me well and got me back on track.

TRANSWORLD

We all went through the 2008 real estate crash. Currently the housing market across the country is booming. You mentioned that in many cases, business properties in Florida have appreciated better than the business. Where do you see this market in a year, two years, five years from now?

ALAN KAYE

I do see some cautionary signs. For instance, everything was selling, but now some things are not selling the first go-around. They're falling out of contract and then having to be re-sold. Number two, some sectors of the housing market are not selling as well as they had been. I think it's like everything else. We have to be a little cautious. It's a great time to buy real estate. There's a tremendous amount of capital, looking for commercial deals, with a minimum amount of well-priced product. Deals that people may have passed on before are being looked at again to see if they make sense.

I think Florida will remain strong, but there's no question that at some point some of the people who moved down here and are buying businesses will feel, "I miss New York. I miss family. I miss change of seasons. I miss all of those things." Some will go back, and if you look at the statistics in New York, it's coming back quicker than people had expected.

Overall, COVID has been a very positive influence for Florida in terms of the markets. I don't see this happening like '08.

Back then, they just turned off the switch one night and things were completely different. Today, mortgages and financing are better than before, although I'm disappointed and surprised to see they're going back to no dock loans, which was one of the main culprits of what happened to us. But I don't know how many of those are being approved, and whether they play with the percentages to make sure that they have some kind of protection.

I think there's going to be a little bit of a slowdown, but the market will remain strong long-term. One thing to consider is the market has become very segmented. Right now, multi-family is the darling. It remains on fire. Industrial is unbelievably hot. There's a minimal amount of space that's available. In retail, the big boxes are hurting with Amazon and other suppliers of goods. But the strip center, which nobody wanted because restaurants were closing, nail salons were gone, has come back faster than anyone expected. So that segment of the market has recovered. Even hotels are coming back.

The one sector that continues to lag is office, and while eventually it will come back a bit, I think that’s the sector of the market that will be hurt most long-term. Many of the firms that needed 20,000 or 30,000 square feet are scaling down to 5,000. People are working remotely, or coming into the office part of the time, and many are still enjoying that, but I think eventually that focus will shift a little. I know a number of employers want their people back in the office.

TRANSWORLD

You've shared a lot of good advice in this conversation. Which leads to our last question. What's the best advice you've ever given someone, whether it's a business owner, a property owner, or both?

ALAN KAYE

That's a terrific question, because with many people in our industry, the way I have to give advice is I will tell them something, and then a couple days later I'll tell it in a different way, and then a third way, and maybe a fourth way, and then all of a sudden, they'll call me and say, "You're not going to believe this, Alan. It came to me in the middle of the night. I know exactly what we have to do here. This is what we have to do." With a straight face, I have to say, "That's a great idea. I don't know how you came up with it."

I think the best advice I've given to certain people is to sell. Never fall in love with the real estate. I understand you may go into it thinking you want to keep it over time, but don't fall in love with it. There are times to sell the dream to somebody else, and move on to something else. I think that that's the best advice I've given, but it's been in different ways. For instance, we just sold a building where the owner did not have good books and records. I told him, "The only way we're going to be able to sell this building is if we make sure we find a buyer who is willing to waive any financing contingency, because a bank won't approve it." It turned out he had tried to sell before. I was his third broker. I did find a buyer who agreed to waive the financing contingency and we closed at a terrific price.

Another important thing is knowing when to buy. One of the top investors in our marketplace had never bought an apartment deal before. He had only been in retail. I urged him to buy a particular apartment building, and he did. Three years later, he told me, "I never really thanked you for pushing me to buy that apartment building. It's one of the best buildings I ever bought. I paid $11.25 million, and I was just offered $18 million for it."

Unfortunately, some people are not receptive to this advice, because sometimes you lose perspective on real estate. You need to have an objective view. What's happening in the marketplace? Are there things that are going to negatively affect your property? You’re not in a vacuum. You have to look at everything that’s going on. New competition could come in next door. You might have a very nice apartment building, and suddenly they're building a new 500-unit, AAA complex with resort-style amenities. That might be a good time for you to sell, before it comes in, and they start to take away your tenants and your occupancy dips. So be focused on everything that's happening in the marketplace, as well as what's happening within the world of your property.

TRANSWORLD

Be aware of what you can control, and look at what you see around you at the same time.

ALAN KAYE

Exactly. You have to watch what's happening with market trends. Which can also help you. Perhaps your building is in the path of progress, and somebody's going to need it as part of an assemblage, so they may pay you more than it's worth for a different purpose. Always be cognizant of what's going on in the market around you at all times.

TRANSWORLD
That’s great advice. Thank you for sharing such great insights for both business and property owners.

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CHAPTER 9

KEEP YOUR PEDAL TO THE METAL

Run Your Business Profitably to the Last Day

Many sellers will feel relieved or unburdened by putting the business up for sale, or when they finally have a signed contract. Often, they start to coast and take their foot off the gas. They cut hours and/or wages, sell off inventory, cancel marketing, or just don’t pay attention, and the revenues and profits start to quickly wane.

This is a huge mistake.

We have often seen right before a closing, a bank or a buyer will ask for the most updated profit and loss statement including the last 30 days. You can only imagine what happens if the financials show a decrease in revenues and profits. The deal dies or needs to be revalued. Even if the buyer is “locked” into the deal, if the trend is bad enough, buyers or banks will cancel the deal, even with deposits at stake.

Conversely, if your revenues and profits continue to improve, your leverage at the closing table is vastly increased. Not that the deal can be revalued necessarily, but it will give you cover for anything else that may pop up unexpectedly. Damaged equipment, inventory shortages, employee loss, valuation challenges can all be "fixed" by having growing revenues and profits.

Have Proper Staff in Place

Having proper staff in place makes a business more easily transferrable to a buyer. The continuity of the business is essential to the buyer's perceived value. The buyer should feel he or she can maintain revenues and profits when you step away using the staff currently in place.

There is a balance to consider. Being chief cook and bottle washer while working 70 hours a week will maximize a business's profits and increase the value. However, this is offset (and then some) by the buyer either not buying because working that hard is unappealing, or feeling the loss of the seller's skills will detract from the profitability of the business.

Therefore, having the proper employees trained in their positions will add value to your business sale. We talked about confidentiality earlier and why we feel it is best not to tell employees about your plans to sell. Once the business is sold, you and the new buyer can meet with employees, and the buyer can convey how important they are to the future of the business. Buyers are usually eager to keep employees. In many cases they even incentivize them to help the business grow.

If you have family members in the business, it can add complications to your impending sale. If the family members are planning to exit after the sale, then the buyer must find suitable replacements. That can be challenging, especially if the family member has a certain skill set and business knowledge that will be hard to replace at the current compensation level.

While we’re discussing compensation levels, we have seen situations where family members have been underpaid or overpaid. If they are underpaid, then the replacement cost must be reflected in the profit and loss recast as the family member is either leaving or will want a fair wage moving forward. If the family members are overpaid and are going to leave, it may be an opportunity to reflect the lower costs moving forward, thereby adding value to the business. But beware: buyers will often push back and continue to voice concern with the operations of the business and resulting profit continuation.

CASE STUDY – ALL IN THE FAMILY

A longtime family business had two of the owner's adult children in the positions of operations manager and CFO. Three other adult children were not involved in the business. The parents wanted to sell the business and share the proceeds with all five children, knowing there would be arguments to succession and estate values tied to the business. We proceeded through the selling process without disclosing the pending sale to any of the children. The buyers wanted to keep the CFO and operations manager but the two decided to leave. The deal barely survived and needed to be revalued to replace the two and offset ramp-up costs.

Lastly and perhaps most importantly with regard to this subject: retaining the seller and/or his or her family is usually not a good choice. Often sellers will not agree with changes a buyer makes and may resent the success the business experiences through the change in leadership. Of course, there are exceptions to this premise. Even in the case of Transworld, Don Parrish stayed on for a dozen years and was an asset to the company and its growth.

The best case for any new business owner is to have good staff in place, all of whom are well-trained in the aspects of the business. They should be well compensated and motivated. The seller should function as a manager, handling tasks that can be easily learned and replaced by a wellmatched buyer. This makes it easy for almost any well-rounded buyer to buy the business.

Have the Capacity to Grow

We often say a buyer pays for profits but buys for the potential. Having the ability to grow is essential to maximizing your value. If your business has no ability to grow due to space, lack of equipment, geography or other constraints, your value to a buyer will be limited to the past financial performance. Most likely, that value will be discounted due to the lack of upside.

Sometimes, even the past financials can be impacted by future needs in capital or operating expenditures such as equipment, software, occupancy, or employee growth/ training. Some examples include:

a) Franchise rebranding or redevelopment requirements in the franchise agreements. Several national chains require a renovation schedule that must be followed.
b) Space constraints on leaseholds or real estate holdings. Moving costs include the physical relocation and lost productivity due to down time.
c) Equipment or rolling stock issues in companies such as landscaping, trucking, manufacturing can be at max capacity.
d) Aging or specialized employees nearing retirement or those requiring a long training or apprentice period. This can also be a concern on the downside if an employee leaves or retires.

CASE STUDY – CRAMMED & JAMMED

We had a distribution business of touristy-type souvenirs that was stuffed into a 5,000 square feet warehouse. You could barely walk through the place. We could not fathom how it passed fire code. Needless to say, the business could not grow in the current space. Buyers were really turned off by the fact they would need to move. The good news was, the business owned the real estate, and it was highly desirable. So, they sold the property and moved the business, which then operated much more efficiently. They immediately started to see the upside potential of growth, which then supported a great price for the seller.

The life cycle of capital equipment, location build-outs, employee training and software should all play into your future plans to sell. There will be an opportune time to sell and offer the buyer enough future growth potential versus the need to make investments that will either delay growth or reduce your business value.

In summary, if the business growth is currently capped, topped out, or facing a near future roadblock then you will have to make the investment needed for the business to continue to earn the profits it has made in the past and have the potential to grow.

CHAPTER 10

SPEND WISELY

Deciding how much money to spend on your business can be difficult no matter where you are in the life cycle of the business. It can be particularly complicated when you know you're going to be selling. When a seller asks us whether to invest in future growth opportunities, new equipment, or hire employees to boost capacity, our response is "What would you do if you weren't selling?" While that may be a simplistic answer, the true decision should be based on how much value the investment will add, and when that value will be realized.

Make Investments Only if Needed to Add Value

If an average business takes nine to 12 months to sell, then the value added should be immediate or at least expected within the next year. Otherwise, speculative investments in facilities, new business lines, equipment, software, etc. should probably be tabled.

If a business line, advertising campaign or new product offering is pursued, and it affects the profitability of the business, it will lower the value of the business. In certain cases, it is possible to end the failed initiative and "recast" the expenses associated with it without affecting the business value. This certainly is not optimal, and many banks will not accept this type of adjustment.

Conversely, if the investment is necessary for the buyer to grow the business, then this kind of investment should be considered.

CASE STUDY – INVESTMENT PAYS OFF

We had a hurricane shutter manufacturer for sale that was considering setting up a second manufacturing line. The existing line was running 24/7 and there were still orders waiting to be produced. This cap on production halted their past growth trajectory and it was determined that the flattening of the sales and earnings would ultimately hurt the value of the business in a sale. The investment in the second line would increase the value of the business well beyond the capital needed for the implementation. The investment was made and the business quickly gained value through the growth of sales and profits.

If the business cannot be sold without the investment, it is imperative that the capital dollars be spent immediately. Examples of this would be a business operating outside of code or even illegally.

CASE STUDY – UP TO CODE

A 50-year-old ice cream parlor had not brought their bathrooms up to ADA regulations. They felt they were "grandfathered in," but that was not the case. But even if they were, a new owner would certainly have to bring the space up to code. They also had portable freezers located outside in the back alley. Let's just say the wiring was not optimal. The two issues killed a multi-million-dollar deal.

In the end, if the investment is required to operate the business legitimately or the value of the improvements will be easily recouped in a sale, then make the improvements. If you're not sure, then make a decision as if you were going to keep the business, as these types of investments cannot usually be "added on" to the value.

For example, if the business is valued at $500,000 based on a multiple of earnings, and you are forced to make a purchase of $100,000 to upgrade equipment that will not drive higher earnings, then the business is probably still only worth $500,000. Perhaps you should not make that investment unless it is necessary to be compliant with laws or it really does affect the salability of the business.

Control, Manage and Document Inventory

Your business should always have an accurate inventory count. We live in a day and age where point-of-sale systems, project management systems, and other inventory management software should be in place in your business. If not, perhaps it is time to implement a system. But again, you must consider the investment vs. increased value discussed previously.

Having the correct, proper levels and accurate inventory can make your business much more sellable. An empty retail store is a red flag as are empty shelves in a factory which will scare touring buyers. Having the business look “full” and successful is important.

Conversely too much inventory can make the business unsellable. This happens often with jewelry stores. If there is $1 million in inventory and the business only has an SDE of $50,000, who is going to invest over a million dollars to only make $50,000? That would equate to trying to sell at a 20-time multiple of SDE.

Also, you must be careful of obsolete inventory. That’s something you may have to liquidate. Just be careful of affecting your normal business revenues and gross margins. It may be best to liquidate it outside of your normal sales channels (eBay, liquidators, auction), and understand if it creates a bump in revenues and income that would not normally occur, that may not be included in your valuation.

There are many articles that cover what the optimum inventory level is for a specific industry or type of business. If there is excess inventory just because you are lazy, or took advantage of some buying opportunities, you can, in the normal course of business, sell it off and get back to a "working level" of inventory and not have to replace it before a sale.

CASE STUDY – OLDIE NOT GOODIE

We were once showing a business and the buyer was walking through the warehouse where there were stacked boxes of inventory. The buyer asked the seller if the inventory was current. The seller assured him it was. They buyer stopped, wiped the dust off the top of one box and noticed it had a 10-year-old manufacture date. Trust was broken, and the buyer never made an offer on the business.

All business sales will include inventory. The level of inventory included should normalize to whatever is required to run the business properly. There should be enough stock on hand so the buyer does not have to buy an excessive amount of inventory beyond the normal course of business in the first 30-60 days of ownership.

When packaging a business, be very careful of how much inventory you "include." Inventory is an asset that is bankable, and therefore any inventory level at the closing below what is included in the sale price could hurt a loan's asset coverage ratio and kill the deal. Make sure you have the amount of inventory on hand that was expressly stated in the business sale package.

Earlier I stated that the inventory level should be a "working" level of inventory. What does this mean? There should be enough inventory at the closing so the buyer does not have to make any "out of the ordinary" purchases. This can get tricky when businesses are seasonal and you are approaching an active selling time for your business. If excess inventory will be needed directly following closing to cover a busy season, the deal will probably survive as many loans include working capital to get through a busy season.

One of the biggest problems we run into with inventory levels is when owners are using a low or no inventory number as a tax saving strategy. This creates a huge problem. Here's how this works.

The formula for
Net Income is:

Gross Sales
– Cost of Goods Sold
= Gross Margin

Gross Margin
– Expenses
= Net Income

The formula for
Cost of Goods Sold is:

Beginning Inventory
+ Purchases
– Ending Inventory
= Cost of Goods Sold

If the final inventory value is artificially lowered, the cost of goods sold is higher and that lowers the net income. Aggressive use of this strategy year after year will often lead to huge amount of inventory being purchased at the end of the year, written off as cost of goods sold, and then stacked in a warehouse or filling the shelves of a business. Ultimately, the inventory number on the balance sheet would be falsely reported as zero - or near zero - to then offset end of the year's profits.

This strategy will save you on taxes as you stack up on inventory and continue to falsely report it as cost of goods sold. But eventually it will catch up with you as you start to sell off the inventory and have no costs of goods sold to report. The result will be an unusually high income for that taxing period. That could even lead to you paying more taxes as you are thrust into a higher tax bracket. The alternative is to keep doubling down and buy more inventory. This strategy eventually becomes unsustainable.

Should you decide to sell your business during this "inventory tax strategy" period, your books and records will be a mess. If you have no records of the correct inventory levels as your fiscal year ends, you will not be able to unwind the inflated cost of goods sold and therefore not be able to calculate the proper net income. When I have seen this in practice, there is never a way to calculate the real Seller's Discretionary Earnings. Therefore, there is no way to assess a proper value for the business. In one case, it made the business unsellable.

CASE STUDY – NOT SHIPSHAPE

Bob owned a boat repair and high-performance engine dealership. At the end of each year, he would take his profits and buy up inventory (classifying it as cost of goods sold) in order to artificially lower his net income. 10 years into his business' existence, he had over $2 million of inventory in his dealership and less than $100,000 on the balance sheet. He wrote off almost $2 million of profits over that time. Since they never officially counted inventory at the end of each year, there was no way to accurately re-create true profit and loss statements for any year. Unfortunately, Bob died suddenly, leaving his widow the task of selling the business. With no profits on the books for the last few years, no bank would finance a sale, and very few buyers would purchase the business at whatever value we could try to assign to the deal. It would be very difficult to start putting the inventory back on the books, as that would cause a huge profitability spike, triggering taxes and unverifiable profits. The widow could liquidate the inventory, but that would also create a large profit, leading to a tax burden. She was really stuck. So, she chose to keep the business and operate it. And just like the old saying "How do you eat an elephant? One bite at a time," the widow slowly sold down the inventory and started to properly document new purchases moving forward. The business did eventually sell, but almost two decades later.

CHAPTER 11

APPEARANCE MATTERS

Keep it Clean

The real estate industry stages homes to help them sell more quickly and at a better price. Your business sale should do the same - buyers will immediately try to picture themselves coming to your place of employment every day and believing they will do so forever. Even though they probably won't be there a lifetime, that is their frame of mind as they look at your office, visit the restroom, look in the warehouse or storage closets. If those places are dirty, crammed with junk or even have bugs/rodents it creates an uncomfortable and unfavorable impression and can even squelch the idea of them buying your business.

CASE STUDY – DIRTY MONEY

a) *We had a commercial linen and laundry service business that looked awful inside. We tried to get the seller to clean up the place but he said it wasn't possible. Every prospect we brought there was turned off by the mess. They make decent money, but it will never sell unless the owner cleans it up.*
b) *We once had a sink in the employee restroom kill a deal. It looked like a hazardous waste site! When the seller cleaned it up, the business sold quickly.*

Knowing all of this, you must clean, paint, declutter and make your business presentable to show. That includes:

a) Painting walls that are old, dark, patched, etc.
b) Cleaning, repairing, and painting the restrooms. Make sure the restrooms are ADA compliant.
c) Replacing any burned-out light fixtures. Also replacing any missing or yellowed plastic lenses.
d) Replacing any missing or water-stained ceiling tiles.
e) Getting rid of bugs, rodents, and hiding the traps that do so.
f) Getting rid of old appliances in the kitchen/breakroom. Modernize this room. It won't cost much!
g) Upgrade signage inside and out. Make sure you are ADA and OSHA compliant.
h) Clean A/C unit vents and returns.
i) Scan old files and get rid of the paper and file cabinets.

There is a lot you can do to spruce up a work environment at a very low cost. Pretend you are a buyer. Drive up to your business and walk through the front door like a customer. What does it look like? What is the first impression in the parking lot or reception lobby?

Take home anything that is personal and “special to you” or is valuable but does not add value to the business.

If you have items on display in your business that are special to you and add no value to the business, do yourself a favor and take them home immediately. We have seen several arguments at closings over items that the seller deemed “personal” but buyers saw otherwise.

A buyer that tours your business will immediately take note of items in the business, and fully expect them to be there the day he or she takes over. Here are some examples:

CASE STUDY – ON DISPLAY

a) An antique mirror in a bridal salon once owned by the seller's grandmother became a huge issue at the closing table. If the seller would have replaced it with a similar decorative full-length mirror before we started the sale process the issue would never have come to bear. We experienced virtually the same story involving a mirror at a tanning salon. It was the seller's mother's mirror that he received upon her passing. He refused to leave it, but the buyer insisted, "no mirror, no deal" as it was the first thing that you saw when you entered the location. To solve the problem, I went out the day of the closing and bought an even nicer mirror. Everyone was happy and the deal closed as scheduled.

b) The first dollars framed behind the counter. A seller claimed it was signed by dear friends, and the buyer thought the seller was being cheap. It got ugly.

c) Signed guitars and other memorabilia that were very valuable. One was a signed Jimi Hendrix guitar. Luckily the first buyers who toured did not buy, and the seller was able to take these pieces home and replace them with similar, nice, but not as valuable rock n roll memorabilia.

d) Antique cash register. The seller said it was a family heirloom. Buyers said it created the character of the checkout counter.

CASE STUDY – ON DISPLAY *CONTINUED...*

e) *We recently had a situation at a cafe where two juicers were on site and the seller wanted to keep one. She revised the asset list in the agreement to reflect this and the buyer protested. The juicer's replacement value was less than $1,000. The seller said there was emotional value and the buyer thought her intention was to compete in near future. The deal died and the seller lost over $150,000.*

f) *A pub owner's wife had given him a leprechaun sitting on a swing. It was displayed above a pool table. The owner passed away, leading to the sale of the business. During the walk-through in the final stages of the sale, the buyer noticed it was no longer there. A very heated argument ensued. The widow refused to let it go with the sale. The buyer threatened to walk and did not show the next afternoon to the closing. The broker tried to locate a duplicate item, but it could not be found anywhere in the metropolitan area. Eventually, an almost identical leprechaun was located more than 1,000 miles away. The broker purchased it and had it sent next-day delivery. The broker did damage control, rescheduled the closing, and presented the replacement leprechaun at the closing. He also served champagne. Both parties calmed down and the deal went through. We're still not sure if the leprechaun or the champagne did the trick.*

Once we even had a painting of Adam Sandler kill a deal! The seller had told us that it was not included in the sale and we did not include it in the list of assets. But at the final walk-through the buyer said, “Where is that Adam Sandler painting?” When the seller said it wasn’t part of the sale, the buyer got angry, told us we had acted in bad faith, stormed out and cut off communication.

Obviously, this only works if the removal of the item does not affect the value of the business moving forward. For example, if you were selling Le Louvre in Paris and wanted to take the Mona Lisa out of the sale, that would probably impact the future of the museum.

Fix or get rid of equipment

Just as personal items in businesses can spark problems, the same goes for old or outdated equipment sitting idle in various states of disrepair and/or functionality. Sellers often get lazy and leave old equipment in the back of the office or warehouse. Buyers see the old piece of equipment as an asset or perhaps a backup to a newer piece of equipment, should it fail. Some even view it as an added capacity because they all have plans to expand your business.

If the piece of equipment is vital to the business or can be used as a backup, the day before the closing is not a great time to find out that it is broken and needs repairs. Time kills all deals and having to postpone a closing due to an equipment repair can really mess up your day. It could be resolved by giving the buyer a “credit” at the closing, but often these credits cost you more than what the repair would be if done by the seller during the normal course of business.

Here are some deal-killing items we've dealt with that fit this description:

CASE STUDY – FIX IT/FIND IT

a) *An old charging station inside a company that sold auto and marine batteries. The old charger was broken, and the seller stated that replacement parts were expensive and rare. The buyer didn't care; it was a great backup to the new charging station. The deal never closed as buyer and seller came to really distrust one another.*
b) *A truck with a cracked windshield. While it didn't affect the truck's operation, it was illegal to operate the truck in the state where the business was located, and the buyer could not find insurance coverage.*
c) *A restaurant deal that fell apart and then resolved over the HVAC. The seller had an old unit on the roof that did not operate, as he never used AC. The buyer wanted it fixed for two reasons. One, under the terms of the lease he was responsible for the unit and the landlord could ask him at any time to make it operational. Two, he wanted to use it and thought it would be an improvement for customers dining at the restaurant.*

CASE STUDY – FIX IT/FIND IT *CONTINUED…*

d) *A seller decided to turn one of the nine Mercedes Sprinter vans into his personal truck and to store it at the place of business. When the buyer found out that this van was once part of the fleet, and now he was being forced to replace it to handle the workload, the deal became very contentious. The seller refused to budge. Eventually the deal fell through due to other minor complications, but the Mercedes was the start of the bad blood and the distrust, and there was no way to get them back to the negotiating table.*

If the piece of equipment adds value, fix it. If it does not, throw it out immediately. But if you do have equipment that is valuable or essential, you cannot get rid of it. Buyers will need everything you have used in the past to make money.

CASE STUDY – CAN'T BE SAVED

We had a dry cleaner for sale. It was not the best business, as the owner was the sole employee, there were minimal sales, it was frequently closed due to travel, and she yelled at her customers.

The night before I was bringing in a husband and wife who were extremely qualified buyers (he worked in the industry, she was the 'business person' who would interact with customers), the seller advised me that she decided to sell the dry-cleaning machine to one of her friendly competitors. Her rationale was "you don't really need a dry-cleaning machine, if you know what you are doing, you can either use the clothes dryer or just outsource it to another dry cleaner."

I calmly pointed out that it is difficult to sell a dry-cleaning business without the dry-cleaning machine, but the deal had been done. So, I worked with her to identify a newer, more energy efficient, and properly sized new dry-cleaning machine to replace the one she sold, and pitched that as a positive to the buyers. I also warned the seller that the buyers would likely adjust their offer to reflect the cost of having to buy the new machine and have it installed.

The buyers made what I thought was a fair offer under the circumstances, but the seller rejected it. Six months later, her landlord terminated the lease. The seller ended up getting pennies on the dollar for her remaining equipment.

If you know it is broken and essential, don't wait till the last minute to fix it. Remember, t*ime kills deals*.

CASE STUDY – SOGGY SAGA

We had a restaurant with a leaky roof. The landlord said the leak was due to improper installation of a hood in the kitchen and the seller was responsible for repairing it. The seller said he fixed it, but the buyer was not satisfied, and said he wouldn't be until the first heavy rain. Since the restaurant was in Utah, where heavy rain doesn't happen often, this would have created a lengthy delay. Fortunately, we had a holdback, and both sides agreed to refund a portion of the holdback to the buyer, so he could be responsible for getting the repair completed to his satisfaction.

CHAPTER 12

EXIT STRATEGY

JESSICA FIALKOVICH, FOUNDER EXIT FACTOR

Jessica Fialkovich is a business exit expert, keynote speaker, small business advocate and award-winning business owner whose mission is to help small business owners leave their legacy and sell their businesses successfully, no matter the size.

Jessica is the Founder of Exit Factor, which provides education and consulting to entrepreneurs buying or selling a business. She is also a co-owner of multiple Transworld Business Advisors business brokerage offices. Her teams have been named the #1 Transworld franchise worldwide and recognized by the International Business Brokers Association for their volume of deals. She is the author of *Getting the Most Money for Selling Your Business* and has been honored by publications including Inc. Magazine and the Financial Times.

TRANSWORLD

Before we zero in on what people need to do as they approach selling their business, to maximize their profits, let's start with your background. You did not take a traditional path to the business of business brokerage.

JESSICA FIALKOVICH

No I didn't. I grew up in a small town called Medford, New Jersey. It was great, we spent our summers at the Jersey Shore. I went to the College of New Jersey, where I got a degree in International Business. I was always an athlete, and thought I wanted to be in the sports world, so I began doing sports internships in college. I started with Pop Warner football, then the Philadelphia Eagles, and after graduating I worked for the Philadelphia Flyers for a few years in a sales administration and database management role. It was interesting. That was right around the time when online marketing and database marketing and email marketing were all converging. My role was to take that and run with it for the Flyers on both the sponsorship and ticket holder side.

I did that for a few years, then met my now husband Al, who was living in Aspen at the time. As a 24 year old, I decided living in Aspen was a lot more fun than Philadelphia, so I joined him there. I did a short stint in marketing in commercial real estate development, but then 2009 happened, at which point we said, "The most secure career path may be owning our own business."

At the time, we had friends that owned a wine store in Aspen. We thought they did really well and had a lot of fun because they drink wine all day, so we decided to do the same thing, but chose to open our store in Florida. That got us back to the East Coast to be closer to family. But that store was never a long-term plan for us, and about three years in we were craving the mountains again and ready to move back to Colorado.

When we sold the store, we dealt with a business broker, and it was not a great experience. We had a good deal financially, but the process was very clunky and really rubbed us the wrong way. That's what led us to get into business brokerage. We saw an opportunity. So after moving back to Colorado we started looking into the industry. We were introduced to Transworld, and knew that was the best fit for us. We've now owned our business brokerage firm since 2013. We started with a small office in Denver, and now we have offices across the state of Colorado as well as Dallas-Fort Worth and Las Vegas.

TRANSWORLD

Let's follow up on something you said. You opened the wine store with the idea that you'd be selling it. One of the biggest mistakes business owners make is not having an exit plan. You knew what your exit would be, but you didn't have a plan for it. As we know, the time to start thinking about an exit strategy is really when you start your business. Talk about why so many don't do that, and how you help them do it.

JESSICA FIALKOVICH

That's a great question. But let me say, I steer away from using the phrase "exit plan." I actually prefer people to think about exit options. As for why people don’t put plans in place, I think a lot of small business owners aren’t big visionary entrepreneurs, they're just very good at whatever they do. They're great technicians, and they build a business around that. They can’t necessarily come up with a vision for their exit. Also, a lot of people think, “No one would ever buy my business. It’s too small.” They don't understand there's this whole other small business market.

So what I try to do is encourage people. You don't have to have this big elaborate plan, but you have to at least know what your options for exit are. That could be selling it to third party, selling to your son or daughter, transition it to your employees, or maybe even it’s just closing the doors. It’s so important to have these options laid out and know which is your preferred choice and which is your backup option.

With our wine store, we didn’t have a plan in mind, but we knew our best option was to sell to someone else, so that’s how we built the business. Knowing the bullseye you’re going for will impact a lot of the decisions you make, such as how you brand the business or how you structure your staff.

I think people steer away from these exit plans because the exit planning industry has built up so much around it. It's like you have to have this pretty plan in a binder and a timeline and research and development, and I don't think any of that's true. You just need to have a bullseye. "I'm heading in this direction." It’s more strategy than plan, and knowing your options.

TRANSWORLD

Which leads us to Exit Factor. Talk about how you started that. It’s a unique niche market. Your Transworld business is booming, but you said, "I want to also do this."

JESSICA FIALKOVICH

After about seven years into business brokerage we asked ourselves, "What's the biggest problem we can solve in this industry?" What we saw was that 95% of our clients were coming to us to sell and they had a definite timeline. "I need to be out in six months. I need to be out in 12 months." Unfortunately, designing the best exit for a small business owner takes time. These owners weren’t just leaving money on the table and selling for less than what the business was worth, they were also reducing the likelihood that their businesses would be sold.

As you know, the statistics vary, but the majority of businesses listed for sale don’t sell. Some surveys say that number is as high as 80%. I think the biggest problem is we don't have business owners thinking ahead enough that they're going to sell. As a result, they sometimes shoot themselves in the foot. But there are little fixes to that.

That was the impetus to starting Exit Factor. We said, “We have this secret playbook as business brokers. We know how to get businesses sold. We know what buyers will pay for and what they won't pay for. If we just open up that secret playbook, we can really change the lives of a lot of our clients by getting them more money or just getting them sold in general versus having to close the doors." We started out with some one-to-one consulting with clients to prove the model, and now we do it in an online environment where we have courses and group coaching and things like that.

TRANSWORLD

We know everyone should be thinking about their exit when they open their business. But there’s a period of time when they have to get serious about it. You can’t just wake up January 1st and say, "By the 4th of July, I want to be out of this business and living on the beach." Obviously it varies depending on the type of business and where you are in your business life, but talk about the time when people really need to get serious. What changes from five years out to three years out to “this is the year”?

JESSICA FIALKOVICH

This is where a lot of business owners get tripped up, because exit planners and others will say, "You need a five to 10 year plan." It’s really hard for people to wrap their mind around that, especially these days where things change so quickly. What's going to happen five to 10 years down the road? I tell people a minimum of two years. A full year of planning, then a year for the transaction to happen. But two years is the minimum. Ideally you’d have three, because when you're getting ready to sell, if you're trying to do some of these value maximizers and increase the value of your business, you're adding another workload onto your plate. It’s not a full-time job, but probably another five hours a week, and even that is a lot for some of these small business owners to handle. So a minimum of two years, but ideally three years.

TRANSWORLD
We’re not going to ask you to give away everything in your course, but there are things any business owner should be doing, knowing they’re leading up to a sale. For example, keeping your pedal to the metal, not taking it easy because they’re planning to sell, instead working harder to grow your business to maximize the sale. What are some of the things people neglect, whether by choice or because they don't realize it?

JESSICA FIALKOVICH
We look at four buckets: exit options, education, financials and owner versus operator. I already talked at length about the first one, and how important it is to know your options.

The second is to educate yourself on the process. As I said, with our wine store we knew we were going to sell, but we went in blind. There's a lot you can glean from learning about how businesses are sold, who buys businesses, and how they're paid for. Knowing that is going to affect how you run your business. This book is a valuable educational tool, so kudos to you for doing it and to business owners for reading it.

The third piece, which business owners hate to talk about, is financials. That’s what really drives a sale, so I’m going to go into some detail. The value of a business is based on your quantitative earnings and the quality of your business. The quantitative piece, earnings, is the bulk of the business. Buyers will look at revenue and they want to see an increase in profits over the time you're looking to sell. The last thing a buyer or a bank want to see is a decrease in revenue or profit over time. So you have to keep that pedal to the metal and show an increase in profit that's reflective of your past history. If you are growing at 20% year over year for 20 years and all of a sudden you're growing at 2% that's going to spark a red flag for some buyers.

Also related to financials is clean books and records. It sounds boring, but it’s critical. I describe it this way: “Your financials are like a scorecard for the business. Buyers will use that scorecard to determine what they'll pay for the business, and bankers will use it to determine how much they'll lend on the business." That part is critical because when you sell, you want to get the most cash at the table. If you have a buyer but banks won’t finance the deal, you’re either looking at a lower sales price or doing some seller financing, which means you get less cash at closing.

Finally there’s the owner versus operator model. Very few buyers want to buy a job. If you want to get the most money for your business, you want to be an owner. So how do you move yourself out of the day-to-day operations and set the business up as a system that generates money, not a job for you? In the course we talk about various things you can do like having the right processes and people in place, designing things like recurring revenue in the business that are desirable to buyers. We go through eight different value drivers in prep to sell. It all ties back to you being the owner of this asset which is a system generating money. You don’t want to be selling a business that’s your job.

This is hard for business owners to wrap their minds around because when we start our businesses, we sit in every single seat. We do everything ourselves. It's something you have to change over time, even if you just do it little by little over time. You can still sell businesses that are jobs, but you’re not going to get the most money for it and you're probably looking at seller financing.

TRANSWORLD

One of the red flags for anyone buying a business is if the owner is wearing all those hats. If they're the sales manager and the marketing director and the chief bookkeeper, a buyer is going to say, "I don't want to do all that." Another red flag is where the revenue is coming from. If one client provides 75% of the revenue, buyers will worry about that client going elsewhere, maybe even going with the seller if he starts a new business.

JESSICA FIALKOVICH

You bring up a really good point. In that education piece, we talk a lot about how it’s not just important to increase the value of your business, you also have to eliminate what I call the deal killers. What if you have to go to market sooner than you planned? Sometimes things happen. People get diseases such as cancer. They get married or divorced. Sometimes something happens that speeds up the timeline. So if we can eliminate the deal killers right off the bat we’re in a better position no matter when we go to market.

A deal killer could be your example, customer concentration. It could be that tax returns weren't filed. It could be legal obligations that need to be cleaned up. A lot of times the deal killer is just aligning your expectations, which comes back to the education of what businesses actually sell for and not pricing yourself out of that market. The bottom line is everything else could be great, if you have one deal killer you're in trouble.

TRANSWORLD
From your perspective, is there a difference between someone selling their franchise versus someone selling an individually-owned business?

JESSICA FIALKOVICH
Not really, except you're entering another party into the process. This goes back to the education pieces, understanding how your franchise handles sales. Some franchises are super sophisticated, and they have a resale department or an outsource relationship with a broker, and they do resales all the time. Some newer franchises might not have done a resale before, so they don't have a process and they're going to be learning through your deal, which is going to slow it down. Then there are franchises that might have a first right of refusal or they might get a kicker on the sales price. We've seen everything under the sun. If you're a franchisee you need to know what's in your franchise agreement.

Ultimately it's just entering another third party into the deal. The hardest part of getting businesses sold is people management, because you have the sell side and the buy side, attorneys on both sides, maybe a banker on one side.

Now you're entering one more person that has a voice, and every additional voice is an opportunity for the deal to die. It's important to have the right advisor and the right broker that can handle all those voices.

TRANSWORLD

You raised a good point there, which is that you can't do this on your own. Someone who's selling their business can't just put an ad on Craigslist and have someone buy it. You need the right team, some of which you should have all along. You should have a good attorney and a good accountant, and I realize we're biased on this, but having the right business broker on your side is a very important component.

JESSICA FIALKOVICH

It's very important. It's crucial to find people that actually do transactional work for small businesses. You and I both use the doctor analogy a lot. If you're having a heart problem, you don't go to your primary care doctor, or a neurologist, you go to your cardiologist. You need the right specialist. In one of our recent deals the seller hired a litigator. That's the worst possible attorney that you could bring into a deal because he's combative. He doesn't do deals very often. He doesn't negotiate very often. He draws a line in the sand and then he fights like a bulldog. Having the right specialty or niche with your advisors is very important.

That's where your broker can help you vet those people. I always tell our clients, "You already have your attorney? Ask him how many small business transactions he's been involved in during the last year." We work with a firm that only does transactional, small business sales. They do several hundred deals a year. Think about how much intelligence and knowledge they're gaining through all those other deals they're doing. That knowledge can help you overcome a challenge in your deal. If you’re not using somebody that's niched into that transactional world, you're losing out on all that knowledge.

TRANSWORLD

Is there a difference between owning your business and your building, versus a business owner who’s renting their property?

JESSICA FIALKOVICH

There's not a significant difference. Owning both does open up the financing box a lot because banks love to finance real estate. It gives the buyer more flexibility on financing. It also gives the owners more options. They may choose to sell the business but keep the building and rent it back to the new owners, giving them an income stream in retirement.

TRANSWORLD

Renting the building is less risky than the owner financing the sale of the business. You talked earlier about some sellers having to finance. Yes, they have monthly income, but there’s always the risk that the new owner could go out of business. They’ve only lost their 20% down. The seller has lost a lot more.

JESSICA FIALKOVICH

It's definitely riskier to do seller financing. As you know, many deals have some seller financing component. It can be as little as 5% of the purchase price. If you can do some prep work in the beginning, you can not only limit that portion, you can also make the seller financing more favorable and protected for you as a seller.

For example, if it's what we call an owner-absentee business, which basically means the owner has no day-to-day responsibilities in the business, we can get an increase in multiple somewhere between 0.5 and two times more. But if we look at it in terms of seller financing, we can say that it’s been running fine without the owner’s involvement. Yes, the buyer could tank it, but the likelihood is if the new owner lets the employees and the management team do what they need to do, that's a better, secure transaction. There are also less risks for the buyer. So the structure of the seller financing note is going to be more favorable to the seller. You could put some more security into it and not have as many downward adjustments written to the note. At times seller financing can be very favorable to a seller, depending on things such as tax treatment of the sale, so making it more favorable for the seller can have its advantages.

TRANSWORLD

What's the best advice you've ever given a business owner and what’s the best advice you’ve ever received?

JESSICA FIALKOVICH

The best advice I give is to just get help. I see a lot of small business owners trying to do it on their own. I think that's a dynamic that's born in us. If you are an entrepreneur, you're usually very independent and sometimes a little bullheaded. This actually ties into the best advice I've ever gotten, which is that you don't have to learn all the mistakes yourself. It's a slow road to growth if you're going to try to make every mistake and learn every lesson on your own without outside help, whether that's advisors or a community of other entrepreneurs. It's a much faster way to growth if you get help from the outside.

TRANSWORLD

As we talk, it's more than 18 months since COVID erupted and changed everyone's lives. It's still out there. We don't know what the year will bring, but I'm going to ask you to pull out your crystal ball and based on your knowledge and experience, tell us, "Here are the trends I'm seeing and here's where I think things are going to go in the next year, two years, five years."

JESSICA FIALKOVICH

It's really interesting. Maybe I'm being hopeful, but I think there's going to be a trend back towards smaller businesses. One important thing we've seen through the pandemic is we need flexibility, adaptability in our businesses because things can happen that we can't predict, whether it's a pandemic or a hurricane or whatever, and the smaller businesses can adapt much more quickly. Although small businesses took the brunt of a lot of the shutdowns and the regulations and things like that, I think they’re going to be the ones that come out on top.

Most shutdowns were in March of 2020. We had a period of uncertainty, but then in May we saw the beginning of a spike in demand for buyers of small businesses or people wanting to start their own small businesses. Bear in mind, there was incentive to buy a business through the SBA. But the incentive ended and the spike continued, and there have been others. So I think the trend is we’re feeling more secure with smaller businesses. Smaller businesses also can do things that workers are starting to come to expect, with flexibility of hours and potential remote work capabilities, and things like that. There's just less bureaucracy. So I think that's going to be a trend.

I also think it will help drive values of small businesses while they're selling, which is also good because we're facing this whole other dynamic outside of the pandemic. That’s the Baby Boomer retirement wave. Depending on the industry, Baby Boomers account for somewhere between 50% and 70% of small business owners. For a few years, that’s been troublesome because we’ve worried, "Who's going to buy all these businesses? Millions and millions of businesses are going to hit the market. Who's going to buy them?"

That’s because for the longest time, Millennials were on this opposite trajectory. They were looking for big corporate jobs or jobs in big tech, but now we’re seeing the reverse happening. The Wall Street Journal called it the “Great Resignation.” The Millennial generation is saying, “I want to control my own life. I want to control my own destiny. I want to own my own business, do my own thing." I believe those are going to happen at the same time, where we're going to see the Millennials pushing to be small business owners and the Baby Boomers wanting to get out, and as a result, it’s actually going to create a really fair market for us.

TRANSWORLD
That's a very interesting projection. Thank you for sharing that, and for sharing so many other insights.

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CHAPTER 13

TIME TO TALK

The first meeting between seller and buyer, which often coincides with the first showing of the business, is like a first date. First impressions matter. If an owner is burned out, and dumps their war wounds on a buyer, it can hurt or even kill a deal. You want to make the first meeting a positive experience for the buyer.

Be Positive During Showings

As we outlined previously, the business should be clean and organized in every way possible. Personally, you should be dressed appropriately for your first meeting. Also, make sure you are in the right frame of mind: friendly, open, and ready to tell your story.

The buyer will ask you questions that cover information you previously provided to the broker. That is normal, as they are looking to get a more detailed accounting of information previously provided to them. Again, it is important to have information that is consistent. They are fact checking the broker as well as you.

CASE STUDY – TRASH TALK

A seller went on and on about how burned out he was. He said his life was run 24/7 by the business, and he couldn't wait to get away from it and relax. He also spent a lot of time talking poorly about his employees. Apparently, he thought he was being honest and building rapport, but his behavior chased that buyer away. He owned the business along with his wife. I had to tell them that he shouldn't be in any of these meetings from that point on, but if he did attend, he certainly had to talk about himself and the business in a much better way.

Full Disclosure

Eventually, if there is important negative information to be disseminated or disclosures to be made, do so at the appropriate time in the meeting. If you have bad news to deliver, make sure you have possible solutions ready to offer.

If the information is critical to the operation of the business, you must provide it to the buyer in writing. Having the buyer sign a receipt confirming that they received the information is an excellent rule to follow.

A business information memorandum that the buyer can sign is one tool you can use. Email is another. Just make sure you get a return acknowledgement of the email you send with the issue clearly outlined.

CASE STUDY – TRAGIC ACCIDENT

An air conditioning company had a very unfortunate accident in its past. One of their employees was in a car accident which resulted in the death of another person. This information was disclosed in the package provided to the buyers once an NDA was signed. We were able to get their legal counsel and insurance company to ascertain the probable level of liability. They created a "hold harmless" agreement and established monies that could be offset if the liability did affect the buyer, and the business was able to be sold.

If you are ever in doubt as to whether information should be disclosed to a buyer, then it probably should. As we say, when in doubt, disclose it!

We have had many deals killed by pending divorces, tax liens, lawsuits and customer issues that sellers tried to conceal. Most issues can be overcome before a closing and understood by buyers if assurances are put into place. Be forthright with your broker at the beginning of the process. We have often seen those specific issues before, and have solutions and connections to get them resolved.

Be Ready to Negotiate

Selling a business involves negotiations. You most likely will NOT receive offers at your asking price. There are exceptions to this generalization, such as when there are several buyers bidding on your business simultaneously, but more often buyers will attempt to buy your business at a lower price and down payment than you are asking.

Should you ask more than what you want to eventually receive? The short answer is yes, but you can't go too high. Data suggests that businesses often sell within 15 percent of the asking price. Therefore, in order not to scare off prospective buyers from making offers, you should make your asking price fairly close to the final price you hope to get when you sell.

The longer answer is: how much time do you have to sell your business? If you are "fishing" for that one buyer willing to pay a premium for your business, that process will most likely take time. Therefore, plan to have at least a year to wait if you are seeking a price higher than the marketplace is usually willing to bear.

But if time is of the essence or your business has issues that a buyer must fix, then you need to price the business to sell.

CASE STUDY – HORSING AROUND

We met with a business owner who had an equestrian distribution business that sold mostly to the horse racing industry. The inventory was huge. The annual sales for the business were about $1 million and the inventory was $500,000. The business only had an SDE of $50,000. The owner was insistent on the valuation of two times SDE plus the inventory added. She said she needed to get that price as she was due to give birth in a few months and she wanted to stay home with her baby. We said that price was most likely unattainable in the marketplace, especially in a short period of time. She refused to list the business and it eventually closed via a liquidation sale. The owner received pennies on the dollar.

Listen to Market Feedback - Get in the Box

The definition of insanity is doing the same thing over and over after it continues to fail. Unrealistic expectation of value by sellers is probably the number one barrier to selling. As you proceed through the process of marketing and selling your business, you will hopefully start to see an offer or two. If you are not seeing offers or have not even had meetings with buyers, your business is probably priced too high.

It could be that your business is not getting to the right buyers, but the ability to find the “one” buyer that will overpay for your business is a long shot at best.

Getting the deal “in the box” refers to back in the old days of Transworld when we used to keep a whiteboard with a list of our offers on it. When they buyer and seller agreed on price and terms and were “under contract,” we would put a box around the name of the business.

Eventually the term getting “in the box” also referred to getting the business price and terms favorable enough to get a buyer to make an offer and get the business under contract. Simply put, getting in the box meant the price would be about two to three times SDE with either a preapproval of SBA type financing from a lender or a 50 percent down payment and owner financing for the balance.

Working with your broker to react to the feedback by buyers and making appropriate changes inside your business and to the offering terms is essential. We do believe there is a buyer for virtually every business; it is often just a matter of price and terms.

We recommend that every 30 to 60 days you review the activity and make adjustments to your offering and how you’re marketing the business. Most of the time is it about price and terms, but sometimes it’s just luck, timing, and the ability for a good broker to find the right buyer.

CHAPTER 14

DUE DILIGENCE

ELLIOTT HOLLAND, PARTNER GUARDIAN DUE DILIGENCE

Elliott Holland is Managing Partner at Guardian Due Diligence, which has evaluated thousands of deals and assisted with more than $600 million in transactions.

Elliott has more than a decade of experience executing middle market deals as an entrepreneur, and has worked for and with the nation's best family offices, independent business buyers, and management consulting firms. The firms he worked for completed billions of dollars in transactions.

Elliott is one of the few deal guys with experience on both sides of the table – on the entrepreneurial side raising capital and the investor side making prudent decisions with capital. He holds an MBA from the Harvard Business School.

TRANSWORLD

Let's begin with a little about you. Tell us about your background and how you got to the world of due diligence.

ELLIOTT HOLLAND

I'm a child of two accountants. They both did business inventory. In fact, what I do is very similar to the work my dad did. However, I didn't go right into accounting. I initially pursued engineering and graduated from Georgia Tech with a degree in mechanical engineering.

I never went into the field, yet spent three years doing strategy consulting with a company called Accenture. Then I got an MBA from Harvard, and got interested in the private equity industry. I recognized that owning equity was the name of the game, and I needed to spin out to actually be able to own some of the equity. I convinced a mentor to work with me and we started a private investment firm called Elsworth Partners. We ran that for three years. We owned an automotive parts company, a tow truck company and a clinical trials business.

Then he retired and I spun out under a different name. In total, I've spent 10-plus years assessing and analyzing deals, and finding due diligence solutions for my deals. I felt the options of the market on that were pretty terrible.

TRANSWORLD

With engineering and finance and business and accounting, you have a very clinical background and an analytical mind, which helps you quite a bit in what you do now.

ELLIOTT HOLLAND
Yes, you could say I'm a nerd cubed. The cool thing about engineering is it's not just clinical. If you asked a theoretical academic what engineers are really good at, they would say analyzing data sets and telling you what they actually mean and scrutinizing what they don't mean when somebody's trying to tell you. We spent a lot of time in the lab recreating some of the fundamental physics principles that we experience every day, not to mention much more complicated ones. We're pretty good at looking at things and saying, "This set of data does not represent this phenomenon you're talking about."

The business of finance is very clinical. I use that aspect a lot now, because I love numbers that line up. I love data sets that have many different lenses to the same situation.

In due diligence, you look at three key data sets for most businesses. You have their financials, their taxes, and their bank statements. Each one is a piece of the pie. It becomes a very nice pie when you can take those pieces, understand what's in and what's out, what's accurate and inaccurate, and provide a picture of a business that's not just based on a single data set, but at least three combined together. I think engineering and accounting might be at that intersection.

TRANSWORLD
Define due diligence when it comes to a buying a business, and expand on those three datasets.

ELLIOTT HOLLAND

To me, due diligence is twofold. One element is if the financials are represented fairly. Because the seller is not typically a financial person. The second piece, which I think a lot of people miss, is whether the business is actually worth what you're paying for it. So, number one, are the financials solid? Once you know they are, number two, is the business worth what the buyer is paying for it? Answering those two questions is due diligence.

The datasets start with the financials. You have to recognize that just because it comes out of QuickBooks doesn't mean it's right. Say you have a guy who sold trucks when he came out of high school. 30 years later he runs a trucking company and owns 100 trucks. He has a bookkeeper he met when he was 21 who really isn't all that great, and at the end of the year that person gives all the papers to their accountant, who gets paid a couple hundred dollars to do the taxes. He doesn't look at any evidence, he just puts together a tax form.

Then a buyer comes in and looks at this and says, "The financials say X." I remind people that X is plus or minus a little bit given who put in the numbers and who checked the numbers. Still, what's nice about the financials is they're the most detailed piece of information. You have all the revenue, costs, profit and accounts receivable. We have all the accounts on the balance sheet. It's a very comprehensive look but still can have fluctuations and movement in it.

The taxes get interesting. Private business owners are particularly good at minimizing their tax burden. What happens is you see a business with revenue that’s similar to what you expect, but way less profit because they run a bunch of personal things through the business. Often you look at the taxes and gasp and say, "Oh, my gosh, it's one half of the profit."

My favorite data set is the bank statements. The reason they’re so great to me is they're static. You can’t walk into the bank and give them $100 and say, “When so and so shows up, tell him it’s $500.” When you have the business bank statement, you can recreate the financials out of an immovable data set. As consumers, we dislike going to the bank to get something done because they’re too rigid. I love that, because it’s rigid in diligence. So, we have the financials, which are typically the highest manifestation of profit for the business, the taxes, which are typically the lowest, and the bank statements, which are usually in the middle and typically closest to the truth.

TRANSWORLD

As we know, one of the important things when a business owner is doing due diligence to get ready for sale is looking for potential deal killers. You talked about the financials. If a business has been steady at around a million dollars of revenue a year for the last 10 years and suddenly it’s dramatically lower the year before they go to market, or even dramatically higher, that can be a problem.

ELLIOTT HOLLAND

Let’s just discuss deal breakers in general. This is also where my engineering mind says loosen up. There are quantitative deal breakers and qualitative ones, and this is a very iterative process too. You start from the biggest ones, where if you saw something wrong, you'd automatically run. If revenue is half of what they said, if they owe back taxes, if there's a lien on the business, if the owner is going to jail for fraud. You have to get through the big ones before even thinking about the rest.

Then you do more of a deep dive. On the financials, did the revenue go up 20% or down 20% and is that believable? Are the assets in good shape or do they need to be replaced? Do you think there's a solid basis to be able to grow the business, because buying it and not growing it doesn't get you a great return. You need to grow it to get the return you want.

During that process, you also get to know the seller and some of the employees in the business, which leads to the qualitative points of diligence. Do you trust the seller? Because for years after you purchase the business, they're still going to know more about that business than you. For that matter, is there a chance the seller is going to compete with you after the deal? Trust is a key component. What about the employees? Do you think the top two or three employees are going to stay or will you have to replace them? How replaceable are they? These are nuanced things.

TRANSWORLD

There are plenty of small businesses that get a big chunk of their revenue from one client. Often that client has been with them for years. How is that addressed in due diligence, and how is it addressed when the buyer looks at it and says, "I'm a little worried here?"

ELLIOTT HOLLAND

That's a great question. Concentration actually comes in many ways. Customer concentration, supplier concentration, even employee concentration, because there may only be one sales person bringing in all the revenue. I would even include industry concentration, because as technology evolves, industries change.

Prudent buyers have to consider that things can go bad. The top salesperson can say he’s going to the guy across the street. The best customer can go to your competitor. If you see risks in a deal, you either walk away or structure them differently so there’s some risk sharing. “I’ll pay you half up front and the other half over three years, assuming that customer stays.”

TRANSWORLD

There’s no exact answer for this next question, because different business owners are in different stages of the lifespan of their business. But at what point do you start doing your due diligence before selling your business? Is it ongoing? Are you doing it from day one? Does it kick into high gear in the last couple years before you sell?

ELLIOTT HOLLAND

The ideal business owner is always looking to sell their business. They're trying to be as good as possible with processes and systems. They're trying to be diversified in customers, suppliers and salespeople. They're trying to keep on top of the industry. But that's probably only about 5% of small and medium-sized businesses. Most people are trying to maximize their revenue, taking as many vacations as they can, put their kids through school, and paying their mortgage.

What smart sellers do is think seriously about selling three years before it's time to do it. If you think about selling as a three-year process rather than, “Let’s get it sold in a year,” it gives you time to fix things that could get in the way. Say you have salesperson concentration. You're able to bring in a new salesperson, train them, do anything that takes additional costs so by the time you go to market, you’ve removed that risk. If you have customer concentration, you can get your salespeople to find new clients and bring them on board so they’re established clients when you sell.

Unfortunately, most people are what I call 11:59, the last minute. They wait until a divorce or a heart attack or a partner disagreement and say, “Okay, we’re going to sell now.” But now there’s no time to make changes that are going to show up. A firm like Transworld is very good at cleaning up those businesses to show them to my clients who are buyers. But you can only do so much if sellers wait until the last minute. If they start the due diligence earlier and fix the issues, they’re in a better position to sell. And that can mean 1.5 to 2 times the purchase price on essentially the same business, where one seller got ready over three years and the other seller waited until the last minute.

TRANSWORLD

So not doing due diligence early enough can be a very costly mistake for business owners. We're biased on this one, but obviously we think another big mistake is not using a business broker. They think, "My business is worth $2 million and I don't want to pay a commission, I want to pocket the whole thing."

ELLIOTT HOLLAND

When you make a mistake selling your business, it can be a seven-figure mistake. It's much more than that five or six-figure commission you don't want to pay. Selling a business is complicated. The only way to really learn this industry is to apprentice under someone else. You may be world class in building a business, but you're not world class when it comes to selling it. That would be like me thinking I can go in and run a manufacturing business as well as the guy who's been doing it for 30 years. You want your business to be represented the best way possible. In fact, I would argue a better brokerage firm can probably increase the price of a business 30% to 50% just in how they package it and how well they manage the process. A good brokerage firm will know how to market your business in the way that a buyer wants to view it, and a buyer will pay more money for a business marketed in the way they want to view it.

Also, you need to look at the length of the process and the challenge of sorting through your options. You don't just list a business on Monday and close on Friday. This can take a year or longer, and during that time the broker helps you understand which buyers are real and which ones are fake, how to respond to the very nuanced things that come into negotiation, and when to pounce. There are even times they’ll say, “You should call this guy personally without me on the phone,” because some deals require that type of conversation. They'll know when those moments are and they'll be able to bring the knowledge of thousands, tens of thousands of processes to analyze and best optimize yours.

Here’s another point. Buyers are very cunning. They can be a teddy bear outside and a grizzly bear inside. If a buyer sees a situation where the seller is a novice, such as the owner without a broker, buyers can take advantage of them in a myriad of ways that even a smart entrepreneur would not perceive.

TRANSWORLD
You're not just bringing a knife to a gunfight, you're bringing a cap pistol to a gunfight. What are some of the other common mistakes you've seen sellers make in those three to five years leading up to the sale of their business, and especially in that last year?

ELLIOTT HOLLAND
They don’t get their finances in order. Here’s an example. Years ago, I was working on a deal in Louisiana. We spent two or three months negotiating a letter of intent. Then the due diligence began. I would get some of what I needed, but it created more questions than answers. I tried to get answers from the seller, who kept telling me, “I’m doing the best I can. I have a business to run.” Which is true, but I’m waiting for

data to help him receive a seven-figure check, and he’s unable to provide the data.

Even early in my career I knew what professional deal makers know, which is that good data comes quickly, and when it’s slow, it’s typically bad. I had a feeling this was going to be bad data. So here I am, pushing the seller for data while also trying to build trust with him. That process dragged on. I had a frustrated buyer, and tension with the seller and broker. There was a negative cloud over the financials, and not enough time to get the best financing for the deal.

I would tell any seller, if your books need cleaning up, get it done. It’s not really that expensive, and it’s money well spent. If you can agree on a purchase price with the buyer, the next day send them the data they need. Not only is it a smoother process, it’s also likely the seller will get a higher price.

Another mistake sellers make is hiding difficult things until later in the process, hoping they’ll be easier to convey. That often hits that trust piece I talked about that blows up deals. Also, sellers can negotiate too harshly. Sellers and buyers need to build trust with the other. If both sides don’t think about building a rapport, it makes closing the deal harder. Then, if the seller is going to stay on and work with the buyer, transitioning the business, that’s not going to be a good working relationship.

TRANSWORLD

One of the things that's difficult to do from a seller's perspective is taking the emotion out of this. They created this business. They built it. Just like someone selling a house, they might have an inflated idea of what it's worth. But as you said, part of due diligence is figuring out what the business is really worth, so they aren't going in with unreasonable expectations.

ELLIOTT HOLLAND

It's important to understand the difference in how a buyer and seller view the valuation of a business. This is a big deal for everybody. The buyer is typically risking more money than they've ever made on a single investment. The seller is giving up the thing that put their kids through college, paid their mortgage, created their freedom, might even have their name on the front door, and they're giving that to somebody they don't know. Emotions run high on both sides. Plus, you can't run a business or be a buyer all that well without having some pride. You've accomplished great things.

I think the ones that get best deals done are able to put aside that hubris, bring humility into the process and get past some uncomfortable things, because they know the end benefit will be worth it. If a seller's expectation is too high and they won't budge, no one will pay it. No reasonable broker will even put the deal in front of the best buyers because the valuation or the terms are crazy.

Yes, the business may have put your kids through college, but the buyer doesn't care. They care about cash flow. Good brokers speak the language of the buyer. If a seller is arguing the value of the business with qualitative things, and the broker can translate them into quantitative, that's what the buyer wants to hear. You just did maintenance on your trucks? Okay, that’s going to save the buyer $50,000 this year. That’s what they want to hear.

TRANSWORLD
We’ve seen a lot of businesses close during COVID. We’ve also seen a lot of new business open up, and existing businesses thrive. If you were to get out your crystal ball, what would you predict for business owners in the next few years? What trends are you already seeing, either with or separate from COVID?

ELLIOTT HOLLAND
Anybody who thought technology was not going to take over every industry was wrong. How quickly it happens and how much your particular business or industry will be impacted is up in the air, but technology has come in. Industrial businesses that made a conscious choice to not spend a lot of time on technology, have to recognize that. If they hold on to the business too long and continue to not focus on technology, even if they're not able to, it's going to be tougher to sell their businesses in five years than it will be to sell them now.

I also think digital sales and marketing is becoming pervasive too. Country club trips, trips to Vegas, sporting event tickets are being replaced in a lot of industries by a website with some forms and some information.

Those two trends are pushing through the small and medium business space. My prediction is that those that can correctly hire somebody who knows technology to come into their business and get that business technology-ready, not perfect but decent, will see an impact.

I'm also going to predict that we’re not only going to see more and more buyers, we’re going to see younger buyers. More baby boomers are going to be selling, and more younger people are going to be buying.

TRANSWORLD
You talked about the horrible experience you had with that deal in Louisiana. Flip side of that, is there one that came together perfectly despite challenges or issues that surfaced during due diligence?

ELLIOTT HOLLAND
This comes back to what I said earlier about taxes showing the minimum profit and the financials showing the highest. One of my clients bought a business, and the broker told us, “The financials showed $100,000 in profit, but we’re going to add back $300,000 that the seller didn’t need to spend, so we're going to call this profit $400,000." I’m looking at a data packet that shows $100,000 of real profit and three times that which we’ll call “I hope so.” This was my client’s first purchase, but he knew this industry well. When I asked him if he wanted to believe all the add backs, he said he thought he could run the business on a much smaller footprint, and wouldn’t be paying for those things. He told me, “Let's get on the phone with them and make sure we understand what their bare bones operations are. Let’s see if that really feels like it's enough to operate the business."

We had a call, and it was a long one, but when it was over, both my client and I understood that even though the add backs sounded facetious in terms of how much they were relative to the core profit, they were actually accurate and there was a much smaller cost basis needed to run that business efficiently. We went from, "This deal is crazy, run to the hills," to "You know what, it's actually pretty accurate. This makes sense." We closed the deal. But it took a little bit of tension and pain to get there.

TRANSWORLD
What’s the best advice you have ever given a business owner wanting to sell their business?

ELLIOTT HOLLAND
Don't be a miser on a million-dollar deal. Use a good broker. The commission is worth it. And pay your accountant a couple hundred dollars to get your finances straight. It’s a good investment to keep you from losing money and trust.

TRANSWORLD
Thank you for sharing that, and all the insights you shared. Your experience and knowledge on the buyer’s side will be valuable to many sellers.

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CHAPTER 15

MONEY MATTERS

Financing the Deal

Financing is a very important part of selling your business and will drive the price you will eventually get. We have seen a 25 percent discount for "all cash." As a seller you might be willing to accept that, but the reality is very few businesses sell without some sort of seller financing.

There is some financing available from third parties. For small businesses, less than $5 million in value, the most important financing source in the United States is the SBA loan program. Banks offering SBA program-type loans will lend typically 80 percent of the value of the transaction, but sometimes even more.

There are many SBA programs, but the most significant are the 7A and 504 programs. For your business to be able to qualify for a loan, the critical factor is the ability for the bank to "see" and value your discretionary earnings. The bank is able to do that when your earnings appear primarily on the front page of your tax returns. The front page of an S-Corp or LLC tax return has line items for owner compensation, interest, depreciation, and net income. When those items are added together and show a significant value, then banks will most often lend.

If your SDE is “buried” in the expenses reflected on the “other deductions” schedule, the banks might take a loan under consideration, but more likely will not recognize buried expense items as income and refuse to loan based on those numbers. So, if all your income is “hidden,” your business will not qualify for financing.

Lenders using the SBA programs often require the seller to have a note in the structure. It gives the bank confidence if the seller has some skin in the game knowing that they will assist the buyer and help them be successful. So even with bank financing, there is still a 90 percent chance you will be holding some paper. Most often we see a 10 percent or so seller note when there is an SBA loan.

One other program that is getting more popular is borrowing from a buyer’s retirement funds. There are strict IRS rules and regulations concerning the structure of this kind of financing, therefore it should only be handled by reputable firms that have vast experience in setting up these loan programs. Benetrends is one such company, but there are others in the marketplace as well.

Other financing by third parties is rare. Asset-backed lending on inventory, equipment, accounts receivables, and credit card processing is sometimes available but can be expensive. In our experience, this is not a significant source of funds, and is rarely implemented.

If your business has challenging books and records, or having financial issues, or other income anomalies arise, then you, the seller, will need to be the bank. Typical seller financing terms are 50 percent down with the balance paid over three to five years at an interest rate at or slightly above current mortgage rates. The payments must allow for a buyer to still earn a living and get a reasonable return on the down payment.

Security on the note is typically a personal guarantee from the buyer, a first lien on the assets, and a collateral assignment of the lease. Rarely is there a lien on any personal assets of the buyer such as a home, securities or real estate. Many buyers are leveraging these assets to gather the down payment for the business.

Are there risks associated with seller financing? Of course, but the failure rate over the years has been low. And if the down payment is near 50 percent, then buyers have a significant reason not to walk away from their business purchase.

It comes down to competition. A buyer has choices and the ability to leverage available cash to buy a business most suited to making money will drive the decision-making process. Here is an illustration of how a buyer’s ability to leverage cash works:

CASE STUDY – OPTIONS FOR FINANCING

Imagine a buyer has $200,000 for a down payment to buy a business. Here are his choices in the marketplace:

a. *Buy a business all cash. Based on a simple two times SDE valuation, a $200,000 purchase would buy a business showing $100,000 in SDE.*
b. *Buy a business with a typical seller financing structure. With a 50 percent down payment, he could lever up to a $400,000 price with $200,000 down. And that business would be netting about $200,000 SDE.*
c. *Buy a business using the SBA loan program with 10 to 20 percent down. Your $200,000 down payment could lever a $1 million purchase. Again, using a two-times multiple, that business would have an SDE of $500,0000.*

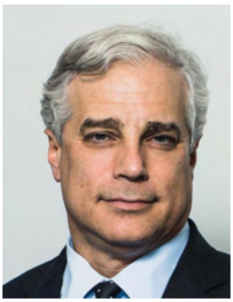
A business valued at $1 million would most likely sell for closer to three times, but this example still points out that businesses seeking all cash are at a huge disadvantage in the marketplace, versus businesses qualifying for SBA loans or that offer seller financing. We have many stories of businesses not selling at all because they refused to offer or qualify for financing.

If you expect to get 100 percent cash at closing you most likely will not sell your business at all.

CHAPTER 16

FINDING THE FUNDS

BARRY SLOANE, CEO NEWTEK



Barry Sloane is the President, Chairman and CEO of Newtek Business Services Corp. Prior to joining Newtek, Barry was a Managing Director of Smith Barney, where he directed the commercial and residential real estate securitization unit and served as national sales manager for institutional mortgage and asset backed securities sales.

Previously, Barry was founder and President of Aegis Capital Markets, a consumer loan origination and securitization business, Senior Vice President of Donaldson, Lufkin and Jenrette, where he was responsible for directing sales of mortgage-backed securities, and a senior mortgage security salesperson and trader for Bear Stearns, L.F. Rothschild, E.F. Hutton and Paine Webber.

TRANSWORLD

Let's begin with a little about you. Talk about your background, your education, and how you ended up doing what you do for business owners.

BARRY SLOANE

I grew up in Brooklyn as the son of a retailer. My dad founded and ran four retail stores, which meant I grew up surrounded by a work ethic where six days a week was normal, seven days a week in season. From an early age, I witnessed what it took to be dedicated, compassionate, and successful to a business and a lifestyle.

I got my bachelor's degree from the University of Buffalo, and a master's and MBA at New York University. Then I was hired by Paine Webber at the very beginning stages of the mortgage and asset-backed securitization craze. I was blessed to grow up in that environment, learning great tools about working with other people and looking at markets growing and maturing. That led me to eventually leave Wall Street and start my second career, which is the financing and providing solutions to independent business owners in all 50 states.

TRANSWORLD

You grew up in an entrepreneurial family. You saw the challenges of being a business owner, but also the success they can achieve and the rewards that come with that. Talk about having that in your background as you now work with all these business owners.

BARRY SLOANE

Being 61, I have a different perspective on the world on family relationships, family support and culture. I've seen changes from my grandparents to my parents to myself to the way kids are today. Historically in America, particularly coming out of the depression, work was an idolized and revered form of activity. Today, in many aspects of American and family life, it’s more thought of something you have to do to pay the bills. Those are not the seeds of successful business owners and entrepreneurs.

TRANSWORLD

You made a choice to start a business that works with business owners. Many are small business owners, who are really the backbone of the economy in many ways. You’ve seen a lot over the 25-plus years you’ve been doing this. What are some of the common challenges you've seen business owners face, specifically in the financing and funding end of it?

BARRY SLOANE

Most small businesses face tremendous challenges, particularly when starting out. Nearly half of them don’t make it five years. Some fail because of a lack of dedication or passion, but many fail because they don’t have a workable plan that allows for dealing with the definite adversities and unexpected consequences that are going to happen to a business. Ultimately, many businesses fail because they don’t have the money to pay their obligations, typically caused by excessive operating leverage or financial leverage.

As businesses look to put their plan together, there’s a lot to think about. Should they borrow the money, should they make this acquisition, should they hire the following people? The list goes on. As they move ahead and hopefully grow, they need to think about whether their plan and their ability to execute on it has an extremely high likelihood of being successful. Some business owners do that, others do it by the seat of their pants. Clearly, I'd suggest the former.

TRANSWORLD

You alluded to one of the big mistakes business owners make, which is to go in without a good plan. But there are many others, which can lead them to financial challenges.

Many people are house poor. They found the house they wanted and stretched their budget to buy it, then six months in it needs a new roof and they don’t have the money for it. How many business owners are business poor? They need to hire people or invest in equipment but can’t afford it. What are the common financial mistakes that can lead to problems down the road?

BARRY SLOANE

I think the key to living a good life is to always expect the unexpected and to plan. The same holds true for businesses. That goes back to overextending financially or from an operating perspective. It’s essential to have foresight. I always tell business owners, “You have to forecast. You must budget. You must predict. You must put yourself in a position where you're never surprised, and you’re always thinking about how to react.”

I look back to my days playing little league baseball. My coach would say, "When you're playing the field and waiting for the next batter to hit the ball, what are you doing? You should be thinking about how many outs there are, and what you're going to do if the ball goes to your left, or to your right, or takes a high hop." It's all about planning out exactly what you're going to do in a myriad of circumstances. That's the difference between being great, mediocre or an absolute failure.

TRANSWORLD

That's excellent advice. Talk about the different types of funding that business owners get when they buy or start a business. Some self-fund, and take the money out of their 401(k). Most borrow the money. They can use a bank, there's the Small Business Administration, and of course there's what you do. Talk about the different types of funding and the advantages or disadvantages they offer.

BARRY SLOANE

Obviously, a good business broker looks at the sources of financing that are available to a business, and what makes the most sense for that buyer. Then the question is what the buyer is going to do with the financing that's available. Is 100% going to the purchase price? Do you need extra working capital to accomplish your objectives so that your plan works? Is the seller going to subordinate a note? They also want to look at more than just the interest rate. Sometimes the flexibility in the loan is more important. How long do you have to repay?

Some businesses are taking out these ridiculous merchant cash advance loans. They're very dangerous because they have short repayment periods. The Small Business Administration provides a loan which may have a higher rate than a bank rate, but it has a 10-to-25-year amortization schedule that drops the payment down. There's no balloon payment and it gives the borrower maximum flexibility to repay the loan.

Also, the covenants of the loan are extremely important. Where an SBA loan has no covenants, bank loans typically have multiple covenants that can be very restrictive to a business owner operating the business. There are clearly many things to think about when it comes to financing your acquisition of a business.

TRANSWORLD
What are the common questions you and your company get from business owners, and what are the questions they never ask but should?

BARRY SLOANE
They should ask about some of the things I just pointed out, covenants and amortization. You never want to borrow money and not have a cushion in case your plan doesn't work out. You don't want to be short liquidity. In fact, you could be in a business that's sub-performing, but if you have a plan to correct that and the liquidity to sustain yourself while that happens, you’ll get through it. The problem with leverage and borrowing money is you can get taken out of the game and the lender forecloses, or you have to go bankrupt. Once

you hand the keys over, you're done. You can't come back. Mapping out contingencies is very important.

The other thing is lenders don't really care about growth. They just want to get their coupon. Realistically speaking, the best loans are made in the worst markets. The worst loans are made in the best markets. In other words, you never want to lend in an overheated market. For example, when the housing market was going great in 2007, it was a bad time to put money in residential housing. If you were a lender with good foresight, you would've pulled your reins in and been more conservative. You would have done terribly in sales but you would have been the smartest lender in the room. There weren't too many smart lenders back then.

TRANSWORLD
You said the best time to do a loan is when things aren’t great and the worst time is when things are going through the roof. Is there a correlation to the best and worst time to start a business? Does it depend on the type of business, or where you are in your life, or a myriad of factors?

BARRY SLOANE
The only way to answer that question is the history is irrelevant. It's all about what's going to happen going forward. Don’t be misled if you’re in the business of manufacturing payphones and you’re so busy you can’t keep up, because the future is there's going to be no payphones.

Similarly, when things are at their worst and there's not a lot of liquidity and despair is all around, the prices of what you're buying are at their lowest. Contrarians make a lot of money in the world and in markets. That’s not to say that if something is going well, you don't want to participate just because it's going well and it might be overheated. It really depends upon what's the future is going to bring. You have to figure out if you’re going to have a problem in your competitive landscape going forward.

Also, you always want to measure your own propensity to take risk. Can I afford to lose this bet? Is it going to wreck my family and my kids' education? Or on the contrary, is this the right time for me to do this? I've taken care of my obligations, I've saved some money, and this is something I’ve always wanted to do.

TRANSWORLD

Let’s talk about COVID. What has the pandemic done in terms of people wanting to sell businesses, wanting to buy businesses, coming to you for loans, coming to you for advice? How has COVID impacted all that?

BARRY SLOANE

What has it done? COVID has taken over all of our lives. What we eat, where and when we go to work, when and how we see the doctor, or just get a haircut. It's taken over everything when it comes to how we live. As far as my area of activity, it's made some people more risk averse but it’s made others more excited about risks. COVID has cost people their businesses, but it has made a lot of people unbelievably rich. It has brought in a factor of change to everyone and everything, and in an extreme manner.

TRANSWORLD

What about someone looking to sell their business, whether that’s now or several years down the road?

BARRY SLOANE

It's a good time for the sellers and they may need to put their money in Bitcoin. For buyers, the best thing you can do is borrow long term money. That’s a huge win. If I’m buying a business, I’m buying it with the real estate, not without, and I borrow long-term fixed trade money.

TRANSWORLD

You’ve shared some great advice with us. What’s the best advice you've given over the years, and what’s the best advice you've ever received?

BARRY SLOANE

That's a tough question. I have to say, the best advice I’ve ever gotten was from my parents. Do the right thing. Have a high level of integrity. The easy road is not the best road. If you do those things, everything's going to turn out fine.

In terms of giving advice, find whatever it is that makes you happy and you like to do, and do that and don't do anything else, because if you're not happy every day, what's the point of living?

TRANSWORLD

You’re in the business of loaning people money to buy a business. Not everyone who applies gets a loan. Tell us about the times when you have to say no, when it’s not a good fit.

BARRY SLOANE

Well, I hate to quote the godfather, but it's not personal. It's just business. You have to eliminate emotion in business. I won’t say 100%, but it has to be pretty close. If you're making an emotional decision, you’d better stop and think about it.

We never have a problem saying no to someone. As a matter of fact, doing that is helping them, because in our opinion, they're not well suited to go into debt. Giving them money when they shouldn't have the money is actually doing them a disservice.

TRANSWORLD

Taking the emotion out of the equation is something we have to do a lot at our end, when someone is selling a business. Maybe they started the business. Maybe they inherited it from their parents. It’s their identity. They have an emotional attachment. But they have to be realistic. We have to help them look at it purely from a business standpoint and say, “Okay, I know my business is worth this much, so that’s what we’ll sell it for.”

BARRY SLOANE

I would imagine business brokers deal with the emotional aspect far more than I do. It must be very difficult at times to get them past what the business has meant to them and their family and say, “Yes, this is the right price.” The knowledge you bring to the table is so valuable to them.

That’s why the best business brokers go above and beyond the transactional aspect of listing a business and getting the most eyeballs on it and getting the best price. You would work to put the business in the best light, and work with the owner to figure out how to maximize the value, how to present the financials, how to unlock certain values, how to reduce expenses, how to grow revenues, how to reduce risk so the business is most attractive. Then on the buy side, it would be finding the right buyer that's the right fit, and not just helping them make the acquisition but then be successful and grow the opportunity over time.

The seller needs to be able to answer questions like, "Is this the best thing for me, for my family? Will I be happy every day? Am I accomplishing my goals by selling my business now?" Many of these answers aren't 100% yes. But they have to be a high enough percentage to make them sure they're doing the right thing.

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WRAPPING IT UP

Okay, now what?

Now that you've read this book, and digested all the information and insights, what's your next step?

Obviously, that depends on where you are in terms of your exit strategy for your business.

If you're still a few years away from selling, you have plenty of time to implement what you've learned in this book. You can take steps to improve what needs fixing, eliminate the deal killers, and put your business in a better position to sell for a better price.

Or, if you're much closer to the time you plan to sell, you may now have a wakeup call.

There may have been times during this book that you said, "I didn't know that." Hopefully, your next thought was, "I'd better do something about that."

No matter where you are in your timeline, there's an important step you can take to get information tailored specifically to your situation.

Because you have this book, you're entitled to a complimentary "Getting it Done" exit strategy session with Transworld Business Advisors. One of our brokers will meet with you, review your business, and help you develop a gameplan. The session is free, the information is priceless. Our contact information is below.

You've invested a lot of yourself into your business. Shouldn't you get the most out of that investment?

To set up your complimentary "Getting it Done" exit strategy session with Transworld Business Advisors:
Call: 800-205-7605
Email: info@tworld.com

To learn more about Transworld Business Advisors:
www.tworld.com

ABOUT TRANSWORLD BUSINESS ADVISORS

Trans-World Realty was formed in 1979 by Gary and Eileen Posner. Sidney Bleich then joined the firm and wanted to specialize in business sales. Sid was from Baltimore, MD worked in the jingle industry and moved to Florida to escape the Northeast winters and stress.

He and his daughter Janine eventually got that division off the ground and wanted to spin off. Sid offered Gary and Eileen the ability to sell him the rights to Transworld Business Brokers and the company was formed by Sidney Bleich about 1982.

Eventually Trans-World Realty closed that office while Sid and family continued to operate Transworld Business Brokers, Inc. Sid was known to meet with every buyer in the corner conference room smoking cigarettes and drinking coffee. He, his wife Greta, and his daughter Janine operated Transworld until his untimely passing in 1991.

Don and Bonnie Parrish bought the briefly idle brokerage and brought some team members from their previous brokerage to initiate their era of ownership. Tom Jones (now a shareholder) and several others were part of the early team.

Andy Cagnetta showed up as a customer in late 1994 and was recruited to join the firm.

After a successful first year, Andy offered to buy the company and the sale was completed in a couple of weeks. His relationship with the former owners flourished for over 10 years. He took the solid 18-year-old company with seven employees and 35 businesses for sale and grew it over the next couple of years.

Eventually seeking to grow beyond nine offices in the state of Florida, Andy and a group of investors considered franchising as a strategy to expand their footprint. In 2010, Transworld Business Brokers, LLC and United Franchise Group, Inc. formed a joint venture to franchise Transworld worldwide. Currently there are over 200 offices throughout the USA and in several countries including Canada, United Kingdom, Australia, South Africa, France, Middle East, New Zealand and others in development. Cagnetta and his shareholders retained the offices in Florida and continue to grow the brand through franchising with his partners Ray Titus and Bill Luce at United Franchise Group throughout the rest of the world.

Now with over 40 years in business, Transworld enjoys a reputation as one of the best business brokerages in the world. With hundreds of business brokers in the organizations and thousands of businesses for sale, Transworld agents have brokered well over 10,000 businesses worldwide and are industry thought leaders. Their unofficial motto “good deals for good people” has been a guiding principle throughout their existence.

Closing the Deal: A Business Owner's Guide to Avoiding Pitfalls, Dispelling Myths, and Selling Your Business the Right Way is a valuable guide for any business owner, whether you're close to selling your business or just beginning to think about it.

Andy Cagnetta shares insights based on his more than two decades of experience running the world's leading business brokerage firm, and has assembled a select group of experts in all the key areas related to selling and buying businesses.

The information in this book will help you sell your business for maximum profit with minimum stress.

ANDY CAGNETTA is the CEO of Transworld Business Advisors, the world leader in the marketing and sale of businesses, mergers and acquisitions, and franchises. During his tenure, Transworld has grown to a worldwide brand, with offices throughout the U.S. and internationally.

Andy is recognized as a leader in the business brokerage industry. He is a past chairman of the International Business Brokers Association and served as state chairman of Business Brokers of Florida.

Andy is involved in numerous philanthropic organizations, and his signature event, "Andy's Family Pasta Dinner," has raised more than $2 million to feed, clothe and help homeless and at-risk individuals.

Andy and his wife Allison live in South Florida. They have two daughters, Lauren and Rachel.

TRANSWORLD Business Advisors

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