Exit, staged right

By Keith Winfree

In Hamlet, there's a famous quotation: "We begin to die as soon as we are born, and the end is linked to the beginning." Although Shakespeare may not have had business exit strategies in mind when putting those words to parchment, the same thought process applies.

We go into business for any number of reasons. To get out of the corporate culture and be your own boss. Opportunity. A chance to pursue your passion as a livelihood. Taking over the family business. The list goes on.

Whatever the reason might be, one common factor exists: We will all eventually exit our businesses. Some by choice (retirement, merger or an offer you can't refuse), some by circumstance (illness, divorce, death or bankruptcy). One way or the other, you will eventually no longer be the one owning and running your business.

Developing an exit strategy really is about a planning strategy. It's a concerted game plan to put your and your company in the best position, from all angles, for the eventual day you leave your business.

WHY NOT HAVING AN EXIT STRATEGY IS AN EXIT STRATEGY

Business owners are often so busy with the day-to-day operations of their business, or they think that retirement is far enough away, that planning an exit strategy falls by the wayside. Essentially, not having an exit plan becomes their exit plan. As long as everybody's health remains intact and no other life-altering events occur (e.g., death, divorce), nobody will know the difference.

Unfortunately, the one thing you can plan on is that unexpected events will occur. Without an exit strategy in place, you're pretty much guaranteed to:

• exit due to outside pressures on somebody else's timetable besides your own;
• undervalue your company;
• pay too much in capital gains and estate taxes;
• fall short of business and personal goals; or
• lose control of the process, one of the key reasons you went into business for yourself in the first place!

An exit strategy is more about planning and growing your business than it is about hanging it up and getting out of the rat race. It's a means to put as much of the control of what happens to your business — the baby you've nurtured from birth — in your own hands.

Having an exit strategy in place will:

• provide a comprehensive road map to successfully exit your privately held business'
• reduce stress and uncertainty on employees and family members (if you have a family-owned business);
• help you control how and when to exit your business;
• generate various options to maximize the value of your business ;
• ensure continuity of your business's long-term survival and growth;
• make sure you achieve both your business and personal goals; and
• preserve family harmony.

With all due respect to Shakespeare, having an exit strategy in place from the time you start your company might be a little extreme, though having a contingency plan in place in case of a life-altering occurrence (e.g., death, illness, divorce) is never a bad idea.

A more realistic timetable for developing your exit strategy is between three and five years, with an additional six to 18 months to execute the plan. Sure, it could be done in less time, but the plan would not be as thorough.

You need time to assemble a team, consider options, and position your company for maximum sale value. You want to start the planning as soon as possible so you, as an owner, can explore options over a longer time frame without being rushed into making decisions, particularly since most exit strategy scenarios involve people in your family or to whom you are close.

There are numerous common exit scenarios. Which of the following have you considered?

• Transferring ownership to a family member
• Selling to other shareholders
• Selling to management (management buy-out, leverage buyout)
• Selling to an employee stock-ownership plan
• Selling to a third party
• Refinancing or recapitalizing
• Going public
• Liquidation

Selecting one of these options and creating the right exit strategy for you starts by sitting down, doing some soul searching and putting down on paper what you want to accomplish with the sale of your business — professionally, financially and personally. There really are no cookie-cutter exit strategies, so the more detailed your goals, the better.

As business growth advisors, we advise our exit strategy clients to follow these steps:

1. determine your end (sale) date;
2. determine your end goals;
3. assemble your team of advisors;
4. communicate your intentions to your stakeholders;
5. collect data;
6. conduct a valuation/analysis;
7. evaluate recommendations;
8. develop a plan; and
9. implement the plan .

Some business owners can handle these steps without a hitch. Most can't. That's why working with a business coach with exit strategy expertise will help get you more in tune with what you want.

It's also particularly helpful when assembling your team of advisors. Your team should include some combination of a business attorney with management and accounting experience, a financial advisor who does estate planning, a tax specialist who knows the latest business tax issues, an insurance professional, an investment banking firm or business broker, and/or a business coach/advisor.

Be judicious in selecting your team of advisors. Remember, they'll be helping you sell one of your most precious and valuable assets, so you want to work with people you can trust, with whom you can have an honest, tell-it-like-it-is relationship. You will also want to work on a fee structure, based on value, provided by seasoned professionals who have been there and done that and have a grasp of the big picture. Most importantly, you want someone who's responsive to what you need.

Besides you, there are numerous people who have a stake in your exit plans. Those stakeholders can include shareholders, family, key employees, major suppliers, bankers and government agencies.

Be very careful when discussing your exit plans. Timing is crucial, as letting the news out prematurely can have detrimental effects on the ultimate deal.

THE NUMBERS

Before working with your advisors to come up with a market value for your business, you'll want to determine what's valuable to you. Namely your life goals, including personal, business, financial, family, and estate goals.

After doing some research in your industry and getting a sense for the marketplace, it's time to work with your advisors to come up with a valuation/analysis to put a dollar figure on your business, and how that will fund your retirement/lifestyle. The valuation/analysis will include:

• preparation of a base-line business valuation;
• a review of your financial needs after the sale and the net after-tax monies you will require to fund your retirement;
• an analysis on how to maximize value; and
• a review of tax strategies.

VALUATION

There are four basic kinds of valuation: asset-based, industry rules of thumb, comparable transactions analysis and discounted cash flow (DCF).

Asset-based is comprised of the net value of assets (assets minus liabilities), the book value, replacement cost, appraised value, liquidation value, and market value of your business.

Rules of thumb is based on industry benchmarks or historical transaction multiples, multiples of earnings before interest taxes depreciation amortization (EBITDA), sales revenue and asset value plus EBITDA.

Comparable transaction analysis involves obtaining information on other similar transactions and recently sold companies.

DCF is usually the preferred method of valuation as it is based on projected future (not historical) operating results, generally over a five-year period. Using this method, you can project future cash flows, develop a discount rate, and calculate a terminal (residual) value.

The valuation/analysis gives your advisors the information they need to come up with a fair market value for your business, and make recommendations on the structure of a deal that would meet your needs. Your advisors should be able to come up with recommendations for more than one exit option, and the pros and cons of each. They should also find ways to maximize value and minimize taxes.

After reviewing the pros and cons of your strategy, you're now in a position to pursue a specific action plan. Before implementing your exit strategy, you'll want to cover a few more bases. First, perform a pre-transaction due diligence with your business attorney. At this time, you'll also be developing a tax strategy with your tax attorney and CPA, and an estate plan with your financial planner, based on the maximum value you could be receiving from the sale of your business.

CONTINGENCY PLANNING

During the entire exit strategy planning and execution, you should have a contingency plan in place in case life-altering events suddenly put your exit strategy into high gear or delay it. The two Ds, death and divorce, can particularly dismantle exit plans, because both potentially involve situations where one or more parties want their share of the business and compensation ASAP.

IMPLEMENTATION

Selling your business is a major, often difficult step for many business owners. The business you helped build is a large part of your identity. Taking the time to develop a sound exit plan and strategy not only makes business sense, but benefits you psychologically and emotionally.

A good exit strategy will offer you the opportunity not only to make the best deal for you and your family, but also to prepare and come to terms with moving on to the next phase of your life.

Does an exit strategy planned and executed correctly ensure a perfect transition to the next phase of your life? Does everything go exactly as you planned it? Probably not. But by working with a seasoned team of advisors and being an active participant in this process, you can come pretty darn close.

Keith Winfree, Ph.D., is the owner of Winfree Business Growth Advisors, based in Louisville, Ky. For further information on exit strategies and Winfree's other business growth programs, including its signature Black Belt System™ 12-step sales and marketing program, visit www.winfree.org.