# The Calculated Exit

## M&A UPDATE | FALL 2021 EDITION

*presented by:*

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Welcome to the fall 2021 edition of The Calculated Exit. Here you will find observations and opinions related to M&A activity as seen through the lens of a boutique transaction advisory group.

## TO DEAL OR NOT TO DEAL?

The topic I get involved in most lately circles around the timing of an exit. It used to be a discussion of the age of the owner, personal goals, the readiness of the business to undergo a changing of the guard. Now these conversations focus more on the markets, interest rates, and most certainly, taxes.

I'm asked questions like:

*"What do you think about tax legislation?"*

*"Is it the best time to sell?" (Notice I didn't say the 'right' time)*

*"What would you do?"*

Well, the question that is on many business owners' minds needs several counter questions to be answered before it can be evaluated in a constructive way.

My questions to you are:

- Are you ready to give up control and still participate in the growth of the business?
- Is your team able to thrive in what will likely be a larger, more corporate environment?
- Is your business mature and stable enough to withstand a productive change in control?
- Are you ready to withstand buyer due diligence and retain your value through negotiations?
- Have you dotted all of your "I's" and crossed all of your "T's"?
- Do you at least know where the skeletons lie and how to evaluate their impact on the deal?

## ARE YOU AND THE BUSINESS READY?

Taxes and interest rates should be part of this analysis for sure, but are you truly ready, and more importantly, is the business ready to be transitioned? If you are the head cook and chief bottle washer and all institutional knowledge rests with you, I'm going to tell you that the business isn't ready. You can change your mind daily, so I'm not going to focus on you here. It takes more than a day to get the business ready, so let's make sure we approach this proactively to obtain the desired result.

## THE IMPORTANCE OF FINANCIAL REPORTING

I'll make this clear; every deal that I have been involved in centered largely around what the business has historically done financially, and what the business forecasts it is capable of doing in the future. Pretty simple concepts, but much less simple when the pains of due diligence set in on an unprepared seller. You must have solid numbers, and you can't get caught ill-equipped. A material adjustment to your reported financial statement earnings can be the kiss of death in a deal. An accountant preparing your tax return is generally not concerned with whether or not your reported net income will withstand a due diligence audit or what is called a "Quality of Earnings" review. Revenue recognition, inventory valuation, missed accrued expenses, and many more items can be easily missed during the tax preparation, and even financial statement review and audit process at times. These items could have a material impact on your earnings and therefore your valuation. You should ask yourself how tight your financial close process is, and how confident are you with your reported earnings?

## DETERMINING ADJUSTED EBITDA

To refresh, EBITDA is Earnings Before Interest Taxes Depreciation and Amortization. This can be calculated straight from your financial statements. Adjusted EBITDA is a step beyond this. Adjusted EBITDA takes into account any and all expenses of the business that are in excess of what the business actually needs to be successful. Examples are:

- Excessive owner's compensation (would someone do your job for less?)
- Excessive vehicle expenses (or personal cars in some cases)

- Excessive travel, meals and entertainment expenses (or personal maybe?)
- One-time or extraordinary legitimate business expenses (lawsuit, 25th anniversary party, failed marketing campaign, etc.)
- Relatives on the payroll that aren't really working and won't go with the aquiring company.

There are countless examples, these are just a few of the most common ones.

Have you done an analysis of these types of expenses for the past 3 or 4 years and the current year to date? You'll need it for your sale of the business efforts when you do plan to move forward with it.

## THE IMPORTANCE OF INTERNAL CONTROLS

Internal controls are procedures and documentation that is put in place for many reasons.

- Safeguarding of assets (cash for instance, but physical assets too, such as inventory, etc.)
- Integrity of the processes and procedures.
- Onboarding new personnel and getting them up to speed.
- Safeguarding against the sudden loss of a key person that handles key business functions.
- Giving the buyer a good look into how you run your business and how secure it is against the risks noted above and many more.

*"Proper preparation prevents poor performance."*

## BE PREPARED

As they say, proper preparation prevents poor performance.

For most business owners, the exit of the business can be the most financially rewarding event of their lives. The question is, why don't more owners focus on this and help maximize the outcome?

## MEET THE EXPERT.

David has been a member of the firm since inception and has been practicing in public accounting for more than 30 years. As the head of the firm's Transaction Advisory Group, he regularly advises CRR clients in buying and selling their businesses, as well as mergers, acquisitions, and joint ventures.

David's skill set is valuable throughout all stages of the transaction process, and through early involvement he is able to help maximize the financial results for his clients. His tactical approach to buyer and seller due diligence enables a smooth transaction process, with a focus on facilitating a well-organized transition for both sides. He also frequently speaks and writes on these topics and hosts transaction related seminars and workshops.

## THINKING OF SELLING YOUR BUSINESS?

Selling your business is a process, not an event. Determining the right time to sell, and finding the right buyer to sell to, can be stressful. There are legal and tax issues to consider, and negotiations can be complex and lengthy. We can help.

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