

Business Transaction Marketplace

Information about Business Valuations, Acquisitions, & Sales

January 2007

Buying and Selling a Business

Welcome to *Business Transaction MarketplaceSM*. Buying and selling a business is a significant transaction for both the buyer and seller. For many, it's a once in a lifetime event. The process can be exciting and financially rewarding, or frustrating and an economic failure. Success or failure is largely dependent on how well prepared and informed you are about process, and what to expect.



The purpose of this newsletter is to educate buyers, sellers and other stakeholders on the variety of issues that surround the transfer of business ownership. This includes issues such as the buying and selling processes, valuing the business, methods to maximize business value, timing the acquisition or sale, preparing a business for sale, categories of buyers, buyer due diligence, financing and tax structuring strategies, negotiating the transaction, post transaction integration, and so on. The newsletter will also discuss certain current economic and other external market forces that are likely to impact business transactions.

By understanding the processes, and anticipating the complexities that may be encountered, we feel buyers and sellers will have more realistic objectives, ultimately leading to what we believe will be more successfully completed business transactions.

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Statistics on Business Ownership Transfers



Business owners decide to sell their business for many reasons ranging from impending retirement, health issues, lack of a clear successor, or simply a desire to pursue other interests. As founders try to decide what to do with their businesses, the Small Business Administration estimates that at any given time, 40% of U.S. businesses face the issue of how to transfer ownership.

The periodical *M&A Today* has reported that "65% of business owners do not know what their company is worth; 85% have no exit strategy." Even more worrisome, it's estimated that business owners have approximately "75% of their net worth tied up in their business".

Unfortunately, a desire to sell does not always lead to an actual sale. The 2005 *Business Reference Guide* reported the following statistics about U.S. businesses offered for sale to third parties during the year:

Annual Sales	# for Sale	Offering Price	# That Sold
\$500K - \$1M	240,000	under \$1M	1 out of 5
\$1M - \$2.5M	138,000	under \$2.5M	1 out of 4
\$2.5M - \$10M	113,000	under \$10M	1 out of 3
\$10M - \$50M	9,000	under \$50M	1 out of 2

It is clear from these statistics that most businesses did not sell. Although the *Business Reference Guide* did not include reasons why, many times it's because of one of the following:

- The business was not adequately prepared for a sale
- The buyer and seller could not agree on price and terms
- The seller did not realize that the marketing and selling process is time consuming and complex

- The buyer often lacked (or failed to commit) the necessary financial resources in order to make the acquisition

Over the coming months, whether you are a buyer or a seller, we hope to educate you on the many issues you will face during the business transaction process. Our goal is to turn the above statistics around, so there are more successful business transactions.

Selecting the Correct Valuation Multiple

The basic formula used for valuing a business is: $Value = Earnings \times Multiple$. Business intermediaries use this formula to determine the most probable selling price of a business that they will market for sale. Although this formula seems simple, the price is often miscalculated because an incorrect level of earnings is applied against an incorrect multiple. The result often leads to a price expectation on the part of the seller that potential buyers will not accept.



Part of the problem is how you calculate earnings. Do you use adjusted EBITDA (earnings before interest, taxes, depreciation, and amortization) or discretionary cash flows? The other issue is what does the ending result include? Does it include the necessary working capital to run the business going forward, or not?

You can read a detailed description of how to properly match the earnings and the market multiple in a recent article that appeared in *IBBA News*, by clicking on the link below. [Read more . . .](#)

Marketplace Alert



At the 2007 New Mexico Economic Outlook Conference, held in January 2007, two speakers provided the following actual and estimated GDP, employment and personal income growth statistics.

U.S. GDP 2007 estimated growth – 3.5%
New Mexico employment growth
2006 – 2.8%
2007 – 2.6%
2008 – 2.8%

New Mexico personal income growth
2006 – 7.1%
2007 – 5.9%
2008-2011 – 5.5%

These statistics tell us that, in the near term, the future looks favorable for the national and New Mexico economies. Both buyers and sellers will be subject to these external factors, and they will play a part in their decisions to buy or sell a business – and when. As the saying goes, “timing is everything.”

Upcoming Darrell Arne Seminar

January 25, 2007, Des Plaines IL

“Tax Boot Camp for the M&A Professional”

Sponsored by the Midwest Business Brokers and Intermediaries

For more information about this seminar, [click here](#)