Preparing YOUR **Business for Transition**

Starter Guide

Volume 1

MEGA

Introduction

As a fully engaged entrepreneur it is wise to stand back and take stock of and evaluate what you have successfully built and calculate the nominal worth of your investment of time, money and effort.

As good business practice you should do this on a regular basis but it is more important to help you during the creation of your mid-long term business strategy, developing tax planning opportunities, selling your business outright, or transitioning the business ownership. It all begins with your current state.

After determining a value for your business, it is time to prepare the business for transition and test the market. Most likely your business is not in 'selling condition', but in daily operation mode. Not unlike your primary residence before you put it on the market It might need staging and refurbishing. So, to maximize your businesses value you need to 'polish' the physical assets, review and organize your regular processes, and business practices, so that outsiders can understand key strategies and components to leverage when you are out of the picture.

"I never invest in any business I do not understand."

- Warren Buffet

97% of business owners feel it is important to have a transition plan... yet only 22% have a plan

Once this is complete and revised you are prepared to test the market and open your business to interested serious buyers. The final value of your company will be determined by a number of factors including things such as; current market conditions, your time table to complete, the buyers appetite, the strength of your business plan and your history of success. Be patient as this entire process may take 12-18 months. Be sure you have a team of advisors you trust and can count on to help you honestly evaluate all offers that you receive. It may have taken you decades to build the business, do not be surprised at the length of time it may take to complete a transition.

This Starter guide is designed to help you prepare and ensure that you can achieve the greatest value for your business, but like any major business project you must build a plan and follow the 5 step process.

UNDERSTANDING THE FIVE STEPS PROCESS:

THE FIVE STEPS PROCESS ARE:

Gather data → Analyze → Prioritize → Plan → Execute

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Mission Statement: to facilitate the transition of a business from one owner to the next, thereby continuing the success of the business for the future.

Step 1

Determine What You Want from the Sale

It's important to think carefully about why you're selling, and what the END GAME is, when you set the sale price.

You may want to seek guidance from a mergers and acquisitions expert or exit planning strategist. This person could also help manage the sale itself and coordinate your other advisors.

Step 2

Complete an Evaluation of Your Business

Many entrepreneurs have an unrealistic idea of how much their company is worth. This means you may have a different value in mind than potential buyers. Even if you're giving the company to a family member. You require an objective evaluation to ease family disputes, plan your estate and optimize your tax treatment.

Step 3

Marketing Your Business for Sale

Decide who you want to sell the business to company Insiders, an outside buyer or family member. Also, consider how much, if at all, you want to remain involved in the business after the transaction as a shareholder, employee or consultant.

You can find buyers by passing the word to your lawyer, accountant, bankers and business networks. You can also work with a reputable business broker. Mega can help, on our new website platform there is a secure area to 'introduce' buyers and sellers in a confidential way. Speak with your BDM as early in the process as possible to gain all our Support in preparation for the transition.

Step 4

Structure the Transaction

Get experts to negotiate the details of the sale. Be prepared to accept compromises on price, timing, your transition participation and asset evaluation

Step 1 Getting Started

At some point in time every organization needs to take stock and establish a fair evaluation of their business.

You may be thinking of selling the business out right, creating a business strategy, transitioning the ownership, or working on development of tax planning opportunities, it all starts with a fair determination of the worth of the business. There are several ways to determine a company's value and we will outline 3 formats. It is important to avoid some common mistakes and to be open to realistic expectations, and evaluations, a third-party professional can help determine the value of and selling price for your business.

Are you selling 1 business or 2?

Do you plan to keep these assets? Sell them separately, or package them in. Evaluate them separately because you never know the end structure of the deal.

- Legal description of building
- Building schematics/plans
- Up to date survey
- Mortgage or lien details
- Latest Property tax info
- Building ownership structure
- Other Equipment

Checklist to prepare an Evaluation:

Selling business only

- Nondisclosure form agreement
- History of business
  - Years in operation, Years in this location, locations, website address, etc.
- Business Structure (ownership)
  Sole proprietor, Shareholders, Corporation
- Untangle legal issues
  - Work with your lawyer to clean up legalese and structure
- Management structure/partnership agreements
  Family operated, or independently managed.
- Have a Vision and Mission statement which defines your business and where it is headed.
- Organizational Chart
  - Staff job descriptions, Tenure on tenor, compensation programs, and other details
- Current business plan
  - Budget, marketing plan
  - Supplier listing and concentration of purchases
- Current Balance Sheet
- Account Receivable/Accounts payable aging Report
- Financial Statements 3-5 years plus interim (if applicable)
- Prior year Tax Return
- Income Statement
- Sales by category and margin
- List of Tangible (equipment, furniture), and intangible assets.
- Customer List
  - E-mails, POS 'dump'
  - Customer addresses to help determine market size and share
- Reasons for selling, available information on market conditions, business trends, risk factors
- Assemble your 'Businses Sale Team';
  Accountant, Lawyer, Business broker, appraiser, real estate rep., as required
- Involve Mega early on - through Credit and your BDM we can help

There are a number of factors that drive value:

Value Adds

- Track records and growth expectations
- Contractual relationships vs. handshakes
- Tangible Assets in good working order
- Proprietary technology/intangibles
- Niche markets
- Barriers to entry
- Strength/depth of management

Value Inhibitors

- Reliance on a few key customers/employees
- Union issues/contingencies
- Outstanding litigation
- Other contingencies
- Complicated/fractional ownership
- Economic/industry risks
- Not willing to commit to a transition period

"32% of business owners have trouble putting a value on their business."

Step 2 Evaluating Your Business

1 **Tangible vs. intangible assets.** All companies have some sort of tangible assets, cash, buildings, inventory, vehicles, etc. Intangible assets are much harder to evaluate and comprise in part of trademarks, brands, customer lists, intellectual property, non-compete agreements, supplier agreements, etc. Generally, it is grouped into what is called Goodwill on the financial statement. It can be substantial if the business has a long and proud tradition with a solid repeat customer base and proven sales success.

2 **Some common pitfalls in preparation for a business transition.** It is common for business owners to have an overly optimistic view of their company's value. They may make unrealistic assumptions about future earnings, buyer appetite or the entire evaluation process. Similarly, the buyer may over or under-estimate the transitional costs, expected synergies and cost savings. To achieve the most favourable outcome and a fair evaluation for your business you need to be ready to share detailed information about the business, expect the value to change based on market conditions, new regulations, sales trends, normalizing non-recurring and discretionary items. Most likely the evaluation will be a range of pricing and the smaller companies may have a wider price range.

Things to watch for during the Evaluation Process

3 **Prepare yourself to face a variety of potential buyers.** Each prospective buyer will have a unique skill set and reasoning for purchasing your business, be aware and understand why they are interested in your company. Do not let emotions overpower evidence, the evaluation process assumes a rational investor is looking to maximize their return. You may need to be open to a purchase that is not 100% cash, it could comprise shares, earn-outs (a note from you), Long term lease on building you keep, or other structure.

4 **When selling a business, offers from buyers are often quite different from the fair market value of the company.** This is because price is not the same as value. Understanding this difference can provide a starting point for pricing a transaction, guide negotiations and temper expectations when the price being offered does not match the result of a valuation. The value is based on assumptions about the market, future expectations, and the potential buyer.

"An evaluation isn't about determining what a company is worth in the current owners hands. It is about evaluating the company's TRANSFERABLE assets."

3 most common approaches to Evaluation

1 Market Based approach takes metrics from comparable companies that have recently sold and applies a multiple based on those companies EBITDA (earnings before interest, taxes, depreciation, and amortization) revenue or other metrics. The quality of this valuation depends on the comparability of the selected businesses and market metrics to your business

Example of a market-based valuation

Comparable company analysis
Public company trading multiples (in 000$)

	Entreprise value	Last 12 months sales	Last 12 months EBITDA	EBITDA margin	Last 12 months sales valuation multiples	
					Revenue	EBITDA
Company A	1,875	1,250	313	25%	1,5x	6,0x
Company B	1,103	900	315	35%	1,2x	3,5x
Company C	1,620	1,200	360	30%	1,4x	4,5x
Company D	1,800	2,000	300	15%	0,9x	6,0x
Company E	5,250	3,000	1,050	35%	1,8x	5,0x
Average				**28%**	**1,3x**	**5,0x**

Values in 000$	
EBITDA	**300**
EBITDA multiple[1]	5.0x
Equity value	**1,500**
Net debt	**(200)**
Equity value	**1,300**

1. Multiple sourced from analysis of guideline public company trading multiples, often adjusted (most commonly discounted) due to size, diversification, growth prospects, or other factors.

2 Asset-based method works with the value of the assets of the business after removing all liabilities, the Net Book Value of the business. Commonly used when selling a business rich in physical assets such as real-estate holdings, equipment, trucks, and owned inventory.

Example of an asset-based valuation

Values in 000$	Book value (liquidation)	Fair value (Adjusted net assets)
Current assets[1]	700	700
Property, plant and equipment, net	350	500
Intangibles[2]	150	200
Goodwill	50	-
Total assets	**1,250**	**1,400**
Current liabilities[3]	500	500
Debt	250	250
Total liabilities	**750**	**750**
Net assets	**500**	**650**

1. Includes cash, accounts receivable and prepaid expenses
2. Could include items such as trade names, customer lists, IP, patents or others
3. Includes accounts payable and deferred revenue

3 Income Based evaluation (also called earnings or cash flow approach) uses projections of the company's future cash flow and assess the risks associated with achieving planned results. This is normally used if your business has substantial goodwill or intellectual property value. It looks at the forecasted revenue and earnings then uses a discounted rate (determined by the 'risks' that may hinder performance) to achieve a realistic future state.

Example of an income-based valuation

Values in 000$	Year					Terminal value
	1	2	3	4	5	
Revenue	**1,000**	**1,050**	**1,103**	**1,158**	**1,216**	**1,240**
% growth		*5%*	*5%*	*5%*	*5%*	*2%*
Gross profit	**400**	**420**	**441**	**463**	**486**	**496**
% gross margin	*40%*	*40%*	*40%*	*40%*	*40%*	*40%*
Operating expenses (excluding depreciation)	100	105	110	116	122	124
% operating expenses, of sales	*10%*	*10%*	*10%*	*10%*	*10%*	*10%*
EBITDA	**300**	**315**	**331**	**347**	**365**	**372**
Less: Capital expenses	(90)	(100)	(110)	(120)	(120)	(100)
Less: Change in working capital	(15)	(15)	(15)	(15)	(15)	(8)
Unlevered free cash flow	**195**	**200**	**206**	**212**	**230**	**264**
Terminal value						1,760
Discount factor of 17%[1]	0.925	0.790	0.675	0.577	0.493	0.390
Discounted cash flows	**180**	**158**	**139**	**123**	**113**	**686**

Enterprise value	**1,399**
Less: Net debt	200
Equity value	**1,199**

1. The discount rate represents the weighted average cost of capital of the company and requires a separate analysis.

Step 3 **Finding the Right Buyer**

Choose the right option

Inside buyer

Pros

- As managers or employees, the new owners are already family with the company.
- Purchases by insiders are more likely to result in a smooth transition, your business legacy remaining intact and employees keeping their jobs.
- Financing is usually easier to secure because of better chances of a smooth transition.

Cons

- May result in lower sale price than selling to an outside buyer.
- More likely to seek vendor financing.

Outside buyer

Pros

- More likely to offer higher sale price.
- May be less likely to seek vendor financing.

Cons

- The transaction may not be as smooth.
- Your legacy could be affected, and employees may be let go if the business is significantly altered after the sale.
- A bumpy transition could lead to delays in the vendor note repayment.

Family sale

Pros

- Your family benefits from your business legacy and is likely to preserve it and retain existing employees.
- The transition will likely be smoother than for an outside sale, increasing the likelihood of repayment for vendor financing.

Cons

- May not lead as high sale price as selling to an outside and more likely to require vendor financing.
- Family tensions could arise if someone feels unfairly left out of the business.

Keep in mind that a mix between these options is possible. For example, you could sell to a management team that includes the owner's children and employees. Another option is airing employees and an outside buyer.

When reviewing potential purchasers BE SURE to check backgrounds and references. During the due process confirm they are SERIOUS potential buyers.

Are you READY to SELL? ASK YOURSELF THESE QUESTIONS:

1. Do you have key staff that can operate your business if you are not there?
2. Does your business have a positive "curb appeal," inside, outside, On-line?
3. Are you ready to disclose all the challenges facing your business?
4. Is your lease transferable and has at least 3 years to run?
5. Do you have 3– 5 years comparative profit and loss statements?
6. Do you have a dispute resolution process?
7. Have you identified the qualities needed in a successor?
8. Are you willing to provide financing or accept any contingent payments?
9. Are you willing to list for 6–12 months?
10. Are you willing to sell the business at 2–4 X earnings?
11. Do you have "Vision" statement? A "Mission" statement which defines the benefit customers can expect?
12. Do you have your "Business Sale team" (accountant, lawyer, etc.) assembled?

Buyer's Checklist

To prepare to buy a business you should ensure that you review this checklist and be in a position to execute a purchase. As a seller you should be aware of what the buyer may be thinking. This is a sample checklist.

Purchasing a Business:

- ☐ Non-disclosure form
- ☐ Identified size and scope of business pursuing
- ☐ Banking arrangements in progress
  - Selected a bank and initial financing approved.
- ☐ Identified regional location preferences.
- ☐ Perform a 'Golden Circle' review
- ☐ Selected Purchase time frame
  - 3-6, 6-9 months, 2 years out etc.
- ☐ Identified Transitional time frame after commitment
  - Purchase as going concern
  - After closeout sale
- ☐ Purchase of assets
  - Building
  - Equipment
  - Inventory
- ☐ Get Financials
  - 3-year financials
  - Current balance sheet
  - Profit and loss statement
- ☐ Identify KPI's for assessment
  - Return on Investment
  - Working Capital Ratio
  - Debt to Equity Ratio
  - Aged Inventory
  - Accounts receivable
  - Retained Earnings shareholder return
- ☐ Review Organizational structure
  - Compensation, Tenor, number of employees
- ☐ Physical store review
  - Last renovations
  - Location analysis

Step 4 Completing the Transaction

5 do's and don'ts when selling a business

5 do's when selling a business

1 Plan ahead

When is it time to start planning your transition? It's never too early.

2 Maximize the value of your business including Planning for the Profit

Many of the steps you will need to complete to get the maximum return from the sale of your business will have to be done well in advance of the transaction. A LARGE part of what you will need to prepare is what to do with the proceeds, to maximize net cash.

3 Keep a cool head and be open to sharing your information

It's easy to become emotional about selling a company you've built from the ground up, but now is not the time to let emotions override good business sense. To sell your business people need to know it is for sale and be able to make a proper judgment on the business. It can be delicate but when the time is right you need to promote your business.

4 Organize your records

Any serious buyer will want to perform due diligence before purchasing your business, and you need to be ready. Documents that need to be readily available include, but may not be limited to, financial statements, minute books, customer and supplier contracts, employment contracts, detailed list and description of assets, outstanding and contingent liabilities, etc.

5 Expect delays and be patient

The sale of a business can be a complicated endeavour. Things such as deal structure (i.e., an asset sale versus a share sale), validating the value of intangible assets (such as goodwill or intellectual property), or the level and type of financing required all add to the timeline to complete a sale.

5 dont's when selling a business

1 Don't choose the price, choose the buyer

I know what you are thinking: "What? Shouldn't I choose the price?" Well, ideally you could have both. But the type of buyer you find can impact the outcome of the transaction, including the purchase price, how much cash you receive at close versus what you may have to defer, as well as the success of the business following the transaction.

2 Don't make yourself irreplaceable

If a business is highly reliant on the exiting owner or cannot function without you, the value will be diminished and it will be hard to find a buyer. Build a strong team that will be in place after you exit.

3 Don't rush things

Taking a bit more time to get things just right will allow you to sell your business at a higher value than if you try to rush things. Also, be empathetic to the buyer's circumstances as they may be dealing with multiple parties, such as lenders and investors, to fund the transaction, while you will only typically be dealing with one party—the buyer.

4 Don't control the relationship with lenders and investors

When it comes to dealing with external financiers, think of it as a partnership and work closely with the buyer to help them get the financing they need to realize the sale. This not only means being ready for the buyer's due diligence, but also for financiers' information requests.

5 Don't do it on your own

Get external advice: A business transition is complex and the stakes are high. Include Mega in the process, we can help.

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Appendix
Getting Started: A Succession Planning List

This list is designed to help you get started on your succession planning journey by thinking about who might take over your business and how much time you need to prepare for your exit.

It's a good time to start talking to your family about your future. Spouses/partners often play a very important role here. If you have not discussed this with them, you will likely be surprised at how many sleepless nights they have had worrying about some of these very same issues.

Write down your answers to the following questions and start having these discussions!

Element		Your notes	Time to complete
Timeline	When would you like to exit the business?		
	How much time do you need to prepare for your exit?		
Contingency Plan	Who could run the business?		
	What income would there be for you and/ or your family to sustain your current lifestyle?		
List of Stakeholders	Family members		
	Business partners		
	Key employees		
	Franchisor or distributor		
Documentation	HR documentation, finances, and contracts with suppliers: are they all in order?		
Estate Planners	What is your desired retirement income?		
	Have you planned for retirement (RRSP, insurance, etc.)?		

Here are some tips to keep in mind when buying a business.

The right business

Go beyond financial statements to ask lots of questions about the business. Start with the most basic: Why is the current owner selling? Is there a hidden problem or is the industry headed for a cliff? Is the company overly dependent on a few customers or suppliers? Are customers loyal to a charismatic current owner and likely to slip away to competitors when he or she is gone? The folks who do well spend a lot of time searching for companies, studying them and, most of all, do not get overwhelmed by their emotions.

The right fit

Make sure the business you're buying has a culture that's compatible with your own. Think of a webdevelopment firm with a free and easy T-shirt and flipflop style. When it was acquired by a buttoned-down telecom giant, it didn't take long for the acquisition to turn sour. "A common and proven practice is to plan a transition of at least six to nine months with the current owner to ensure the transition is made gradually and smoothly," says Mignacco.

The right price

Do your homework on what businesses are selling for in your industry and region. It's important to be disciplined about how much you pay, even if your bankers are willing to lend you more. Overpaying will reduce your financial returns and increase your risk of default. "You shouldn't hesitate to consult experts, such as accountants or lawyers, to make sure you pay the right price," says Mignacco. "They sort of act like the inspectors or appraisers we hire before buying a house. It's a worthwhile investment."

The right advice

If your internal team is less experienced or busy on other projects, an external team could be brought in for support. They will help you be more objective with due diligence and may prevent you from turning a blind eye to major defects. For example, professionals from audit firms can assist you in the due diligence review of the target company's financial results, accounting procedures, working capital management or contingent tax liabilities. A lawyer specializing in mergers and acquisitions, meanwhile, can advise you on common acquisition agreements, information technology and human resource management practices.

The right financing structure

Remember to finance your acquisition in a way that maximizes repayment flexibility. Besides a loan secured on the assets of the company, you should typically seek financing from the existing owner. Vendor financing usually comes with a reasonable interest rate, flexible repayment terms and no personal guarantees. To round out the financing, consider growth and business transition capital because it also features flexible terms and usually requires limited or no personal guarantees. The mix of financing tools that you use can dramatically change the return you realize and what kind of risk you're facing in the company and personally.

The right mindset

Patience is a virtue, especially in a hot market. The September 2017 BDC report *The Coming Wave of Business Transitions in Canada* showed that four out of 10 Canadian small business owners are considering divesting their business over the next five years. This should tip the balance in favour of buyers.

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Appendix
Project Planning Template

This may be the most important single project you ever undertake as an entrepreneur. Take the time to build a proper project plan and execute the plan. Select a team and define their roles and responsibilities.

1. SUMMARY OF PROJECT INFORMATION (CHARTER)

Project Name: ______________________________

Summary Description: ______________________________

Project Leader: ______________________________ Project Sponsor(s): ______________________________

Team Members:	Roles & Responsibilities:

Project Start Date: ______________________________ Completion Date: ______________________________

Last Revision Date: ______________________________

2. INTRODUCTION, OPPORTUNITY, OBJECTIVE & SCOPE

3. ASSUMPTIONS & RISKS

*

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Project Planning Template

This may be the most important single project you ever undertake as an entrepreneur. Take the time to build a proper project plan and execute the plan. Select a team and define their roles and responsibilities.

4. RESOURCE REQUIREMENTS & COST

Description:	Cost
TOTAL COST	

5. BENEFITS

Description:	Benefit
TOTAL BENEFIT	

6. POST PLAN SUCCESS MEASUREMENTS

Key Performance Indicator	Current State	Target

7. MAJOR PROJECT MILESTONES

Description:	Target Date

8. PROJECT APPROVAL

Project Sponsor: ______________________ Date: ____________

Signature: ______________________

*All Projects must have a Project Action Register Completed. See next page (3 of 3)

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This may be the most important single project you ever undertake as an entrepreneur. Take the time to build a proper project plan and execute the plan. Select a team and define their roles and responsibilities.

TIMELINE

Project Name: ______________________

Description: ______________________

Project Leader: ______________________

Team Members		

Project Start Date: ______________________

Completion Date: ______________________

Last Revision Date: ______________________

#	Description	Deliverable	Owner	Due Date	Status	Comments
1						
2						
3						
4						
5						
6						
7						
8						
9						
10						
11						
12						

* Appendix - Commercial Property Listing Sheet

This is a sample template if you are selling your building as well, so that the property can be quickly assessed by the potential buyer and you can concentrate on the more complicated portion of the sale.

Date Listed

Listing No.

LISTING DETAILS

Listing Status: Active Pending Sold Let Archived

Branch

Listing Type

Agent 1

Agent 2

Agent 3

PROPERTY DETAILS

Price Per m^2

Gross Price / Rental

Municipal Value

Unit No.

Floor No.

Complex Name

Erf No.

Street No.

Street Name

Country

Province

Area

Suburb

PROPERTY TITLE

Freehold Sectional Title Share Block Leasehold

ZONING

Industrial Commercial Agricultural Retail

Floor Size (m^2)

Land Size (m^2)

PROPERTY TYPE

B & B Building Business Factory Farm

Hotel Industrial Yard Investment Mini Factory Office

Retail Showroom Vacant Land Warehouse

Tender Auction Bank Repossessed Distressed

Extras

Offers From

Offers Increment

PROPERTY FEATURES

Office/s (m^2)

Price Per m^2

Office Space Total Cost

Retail (m^2)

Price Per m^2

Retail Total Cost

PROPERTY FEATURES

Factory/Warehouse (m^2) | Price Per m^2 | Factory/Warehouse Total Cost | Grand Total

Yard (m^2) | Price Per m^2 | Yard Total Cost

Rates

Yard Access

Building Height (m) | Floor Loading Capacity (Tn/m^2) | Security | Air Conditioning

3 Phase

Power Notes

Amps

Occupation Date | On Transfer | Immediately | Negotiable

Open Parking Bays No. | Cost / Bay (Ex VAT): R: | Total Cost (Ex VAT): R:

Covered Parking Bays No. | Cost / Bay (Ex VAT): R: | Total Cost (Ex VAT): R:

Parking Notes

LEASE DETAILS

Lease Period | Available From | Deposit | Annual Escalation (%)

Lease Includes

Lease Excludes

Lease Notes

RATES & LEVIES

Levy / Month (ex VAT) | Rates / Month (ex VAT) | Estimated Monthly Rental Income (ex VAT)

GENERAL PROPERTY REMARKS

SELLER / LANDLORD DETAILS

Title | First Name | Last Name

Home Tel | Work Tel | Cell

Address

Fax | Email

If Owned By Company Or Trust

CC | Pty Ltd | Trust | Other

Entity No.

Entity Name

VAT Number

Entity Postal Address

VIEWING DETAILS

Viewing Contact Person | Viewing Contact Number | Viewing Keys Available From

Viewing Instructions

WEBSITE DETAILS

Marketing Heading

Website Description

YouTube ID | Virtual Tour URL

Date:________________ Signature:__________________________

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Appendix
Notes

Step 1
Getting Started

Step 2
Valuating Your Business

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Appendix
Notes

Step 3
Find the Right Buyer

Step 4
Complete the Transaction

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