

OPPORTUNITY IN SIGHT

Maximize Your Exit Later by Planning for it Today

KNOWLEDGE

Learning Objectives

Identify your level of
readiness for a
successful exit

List the steps in the
exit planning process

Compare strategies to
grow before, during
and after transition



FUTURE CONTENT

Stay Tuned!

1. Process & Systems (Tech Stack) Improvements to Increase the Value of Your Business
2. Preparing Your Financials for the Sale Process
3. Preserving Your Wealth - Tax Estate Planning Considerations

... And more!

AREA OF FOCUS

Today, We're Covering

Navigating Disruption, Empowering Operations & Digital Transformation

QUICK TIPS

Zoom Webinars

Ask Questions in Q&A Box

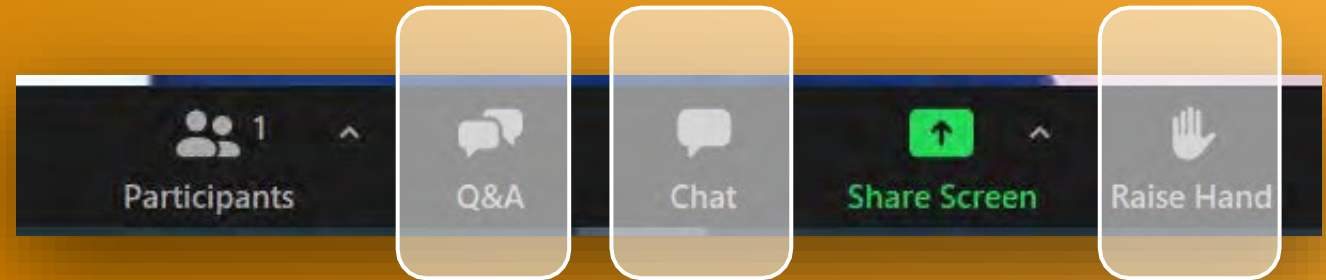
- Click the Q&A button to open the window
- Type your response in the text field
- Click Send

Chat

- Click the Chat button to open the chat panel
- Type your message in the Text box at the bottom of the panel
- Press Enter to send your message

Raise Your Hand

- Click the Raise Hand button at any time to indicate to the host know that you have a question or need assistance
- To lower your hand, click the Lower Hand button

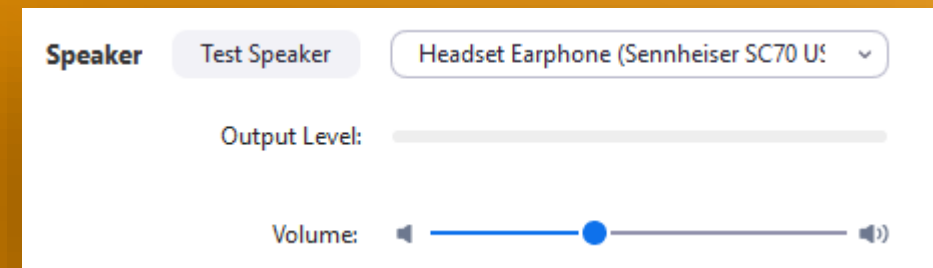
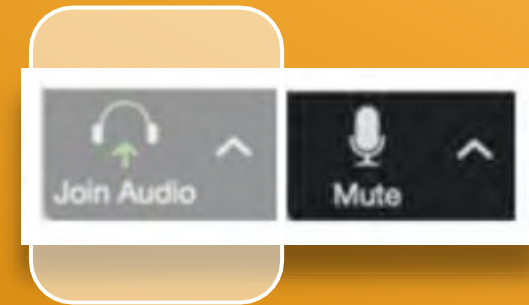


QUICK TIPS

Adjust Audio Speakers

Audio Options

- Click Audio Options - this will open your audio settings
- Click Test Speaker to play a test tone
- If you cannot hear it, select a different speaker from the menu
- Try adjusting the Volume



OPPORTUNITY IN SIGHT

Maximize Your Exit Later by Planning for it Today

WELCOME

Today's Presenter



PARTNER
Armanino Advisory LLC

Bryan Graiff

✉ 314 983 1309

Bryan.Graiff
@armanino.com

WHAT WE'LL COVER

Agenda

- The Current State of Exit Readiness
- Increasing the Value of Your Business
- Preparing for an Exit
- Tax Implications of an Exit
- Q&A

The Current State of Exit Readiness

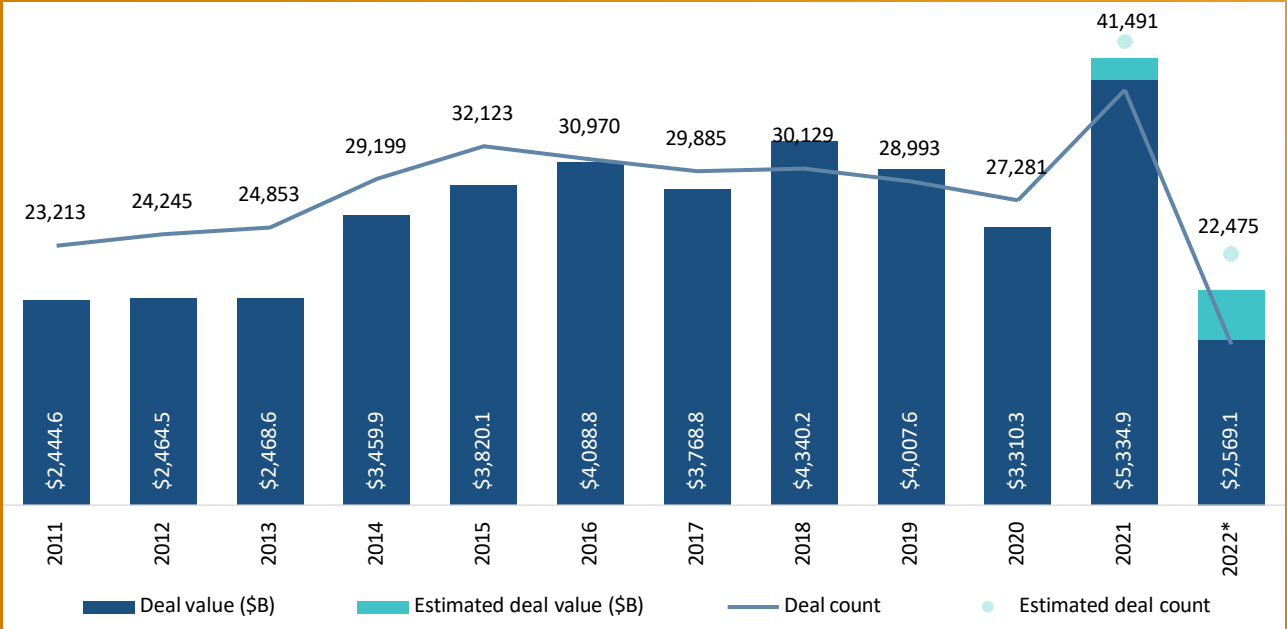
Polling Question #1

Do you currently have a plan in place for an exit?

- a) Yes
- b) No
- c) N/A

MARKET ACTIVITY

Global M&A Activity

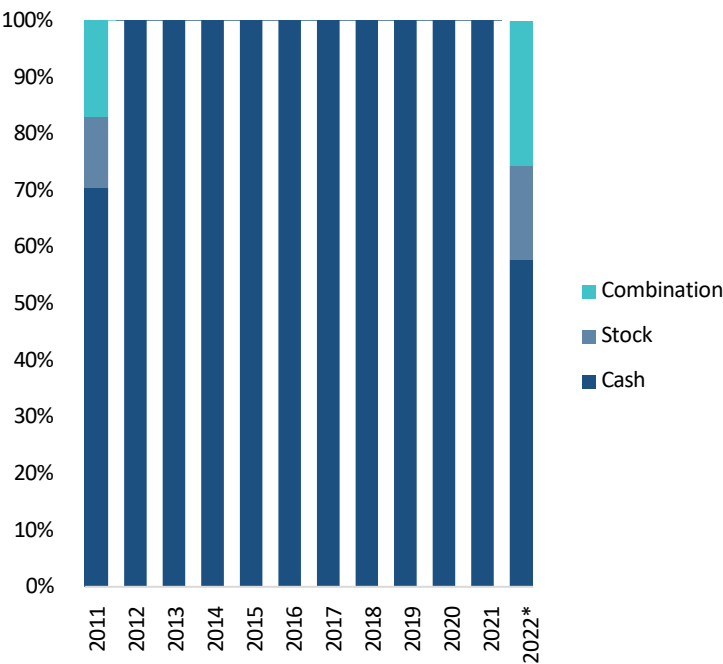


Source: Pitchbook
*As of June 30, 2022

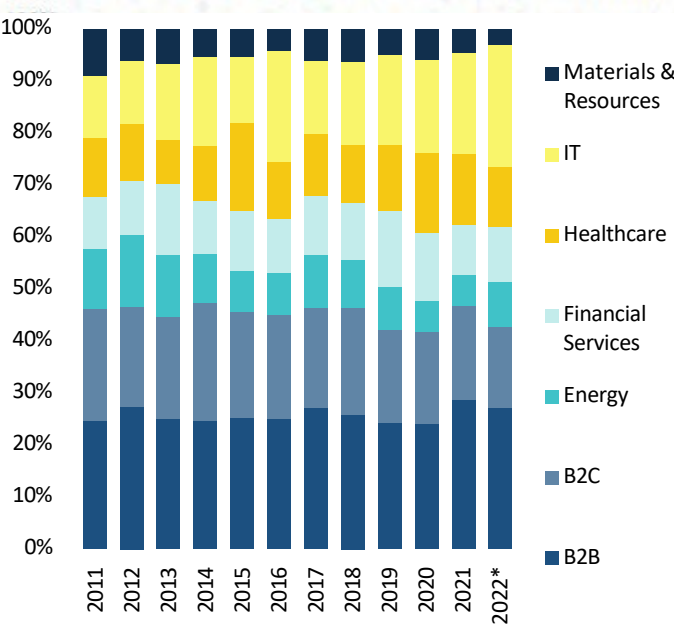
MARKET ACTIVITY

Global M&A Activity

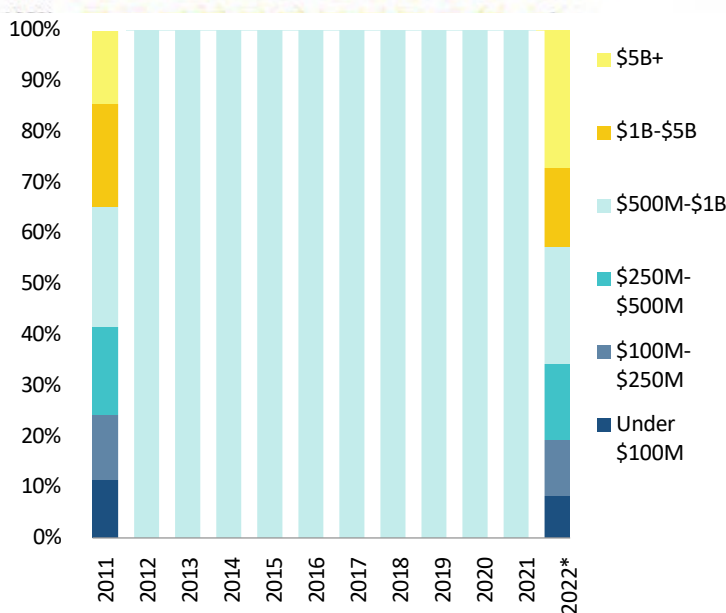
M&A deal count by payment type



Share of M&A deal value by sector



Share of M&A deal value by deal size

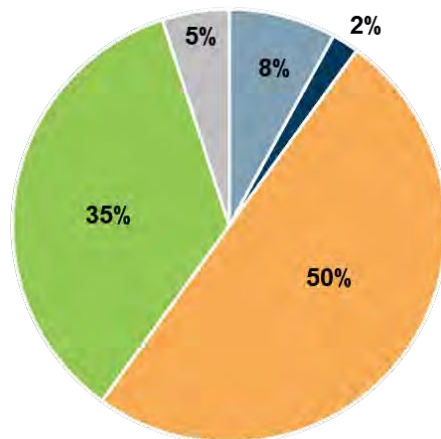


Source: Pitchbook
*As of June 30, 2022

THE CHALLENGE

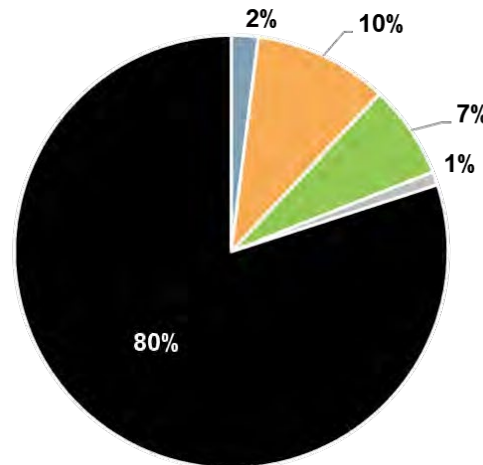
State of Owner Readiness

IDEAL ALLOCATION



REAL ESTATE CASH
BONDS STOCKS
OTHER

OWNER ALLOCATION



REAL ESTATE CASH
BONDS STOCKS
OTHER BUSINESS

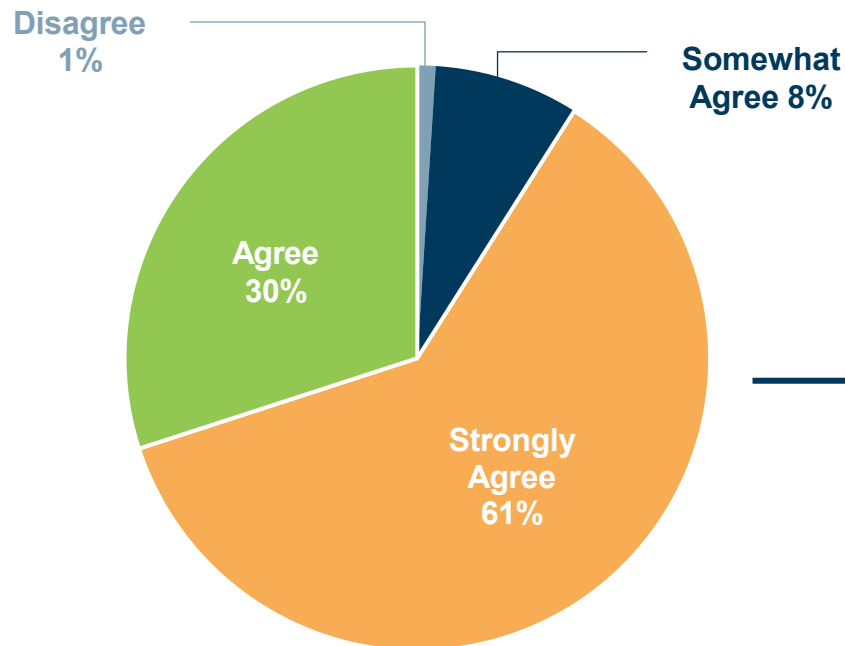
NEARLY 80% OF BUSINESSES PUT ON THE MARKET DO NOT SELL, NEARLY HALF OF THOSE SELLING WITH SIGNIFICANT OWNER CONCESSIONS.

12 MONTHS AFTER SELLING, 3 OUT OF 4 BUSINESS OWNERS SURVEYED "PROFOUNDLY REGRETTED" THE DECISION TO SELL THEIR BUSINESS.

ONLY 30% OF ALL FAMILY-OWNED BUSINESSES SURVIVE INTO THE SECOND GENERATION, 12% INTO THE THIRD

99% of owners **agreed** with this statement:

“Having a transition strategy is important both for my future and for the future of my business.”



And yet...

The very same surveyed owners reported the following data which proved contrary to the statement that readiness was actionably important:

79% OF OWNERS HAVE **NO** WRITTEN TRANSITION PLAN

48% HAVE DONE **NO** PLANNING AT ALL

THE SOLUTION

Exit Planning

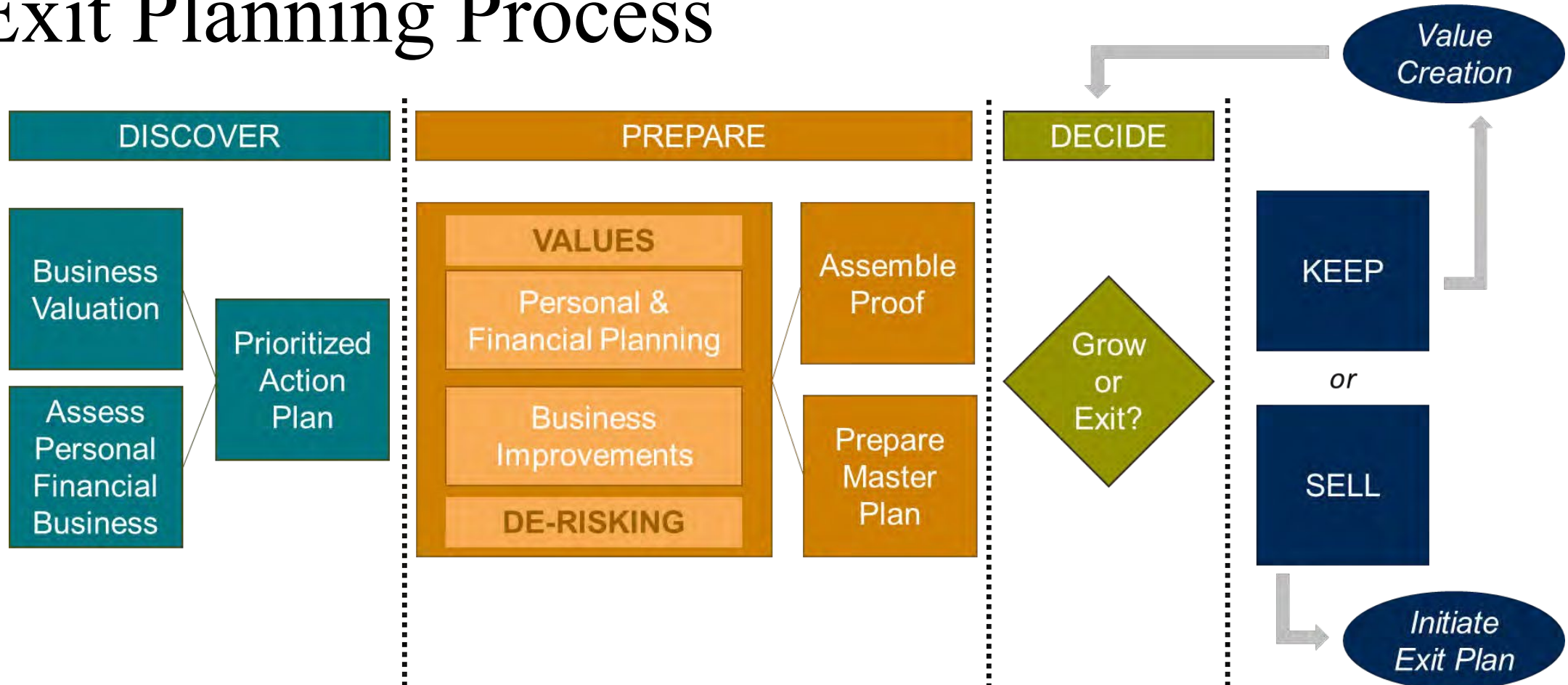
Exit planning combines the plan, concept, effort and process into a clear, simple strategy to build a business that is transferable through strong human, structural, customer, and social capital. The future of you, your family, and your business are addressed by exit planning through creating value today.

Exit planning is
BUSINESS STRATEGY

“You really only have 2 choices, you can plan for your exit or not plan, but eventually you are going to exit”

GETTING STARTED

Exit Planning Process



How Much Is My Business Worth

versus

How Much Will Someone Pay for my Business

Polling Question #2

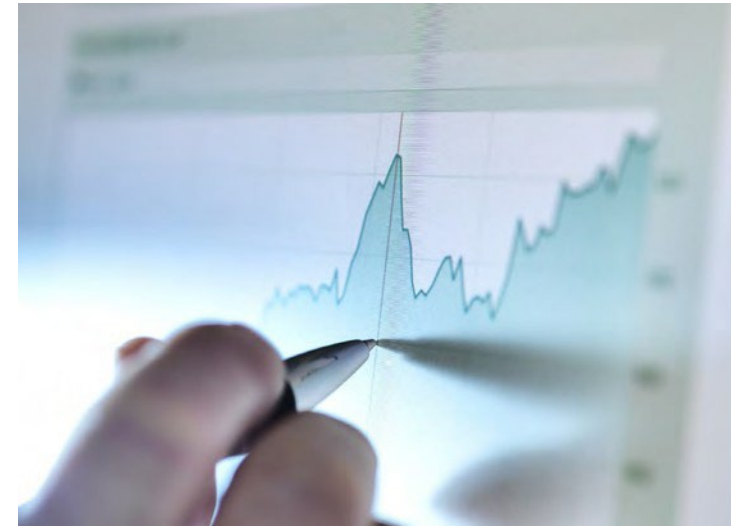
How confident are you that the valuation of your business would be fair?

- a) Very
- b) Somewhat
- c) Not at all
- d) N/A

VALUATION

The Purpose of Valuation

- Is the business saleable and what should it sell for?
- Determine a starting point for negotiation
- Determine characteristics that “add” and “detract” from value
- Not here to issue an “opinion of value”
 - Real estate agent vs. appraiser analogy



VALUATION

The Process of Estimating Value

- Review 3 years of monthly financial statements
- Analyze the company's operations
- Research the company's industry
- Estimate the company's adjusted cash flow
 - High level adjustments
- Search for industry valuation multiples
 - Deal Stats, Capital IQ, BRG
- Consider "value drivers" specific to the company
- Apply market-based multiple to subject company metric



MAXIMIZING YOUR METRICS

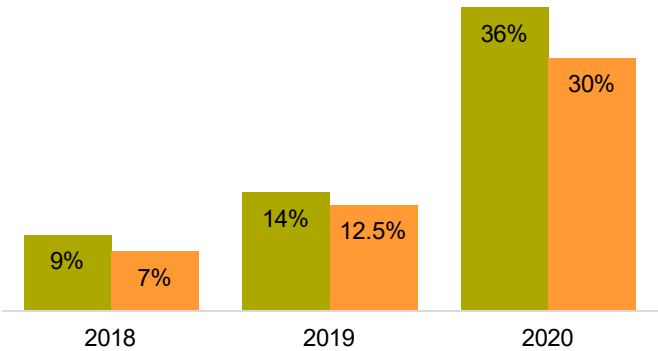
Metrics Buyers Use to Value Businesses & How to Maximize Those

- Competitive Value Benchmarks
- Entity Value Drivers
- Valuation & Growth Potential
- Entity Valuation Opportunities

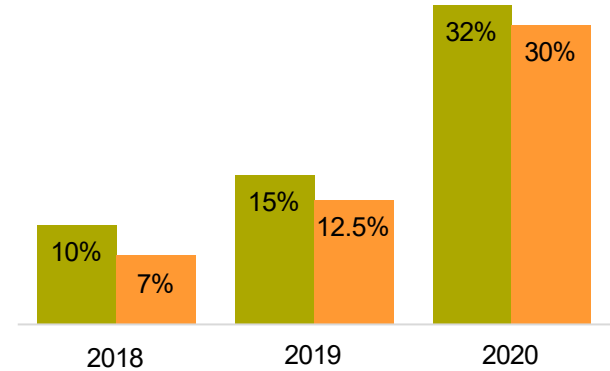


COMPETITIVE VALUE BENCHMARKS

Revenue Growth YOY

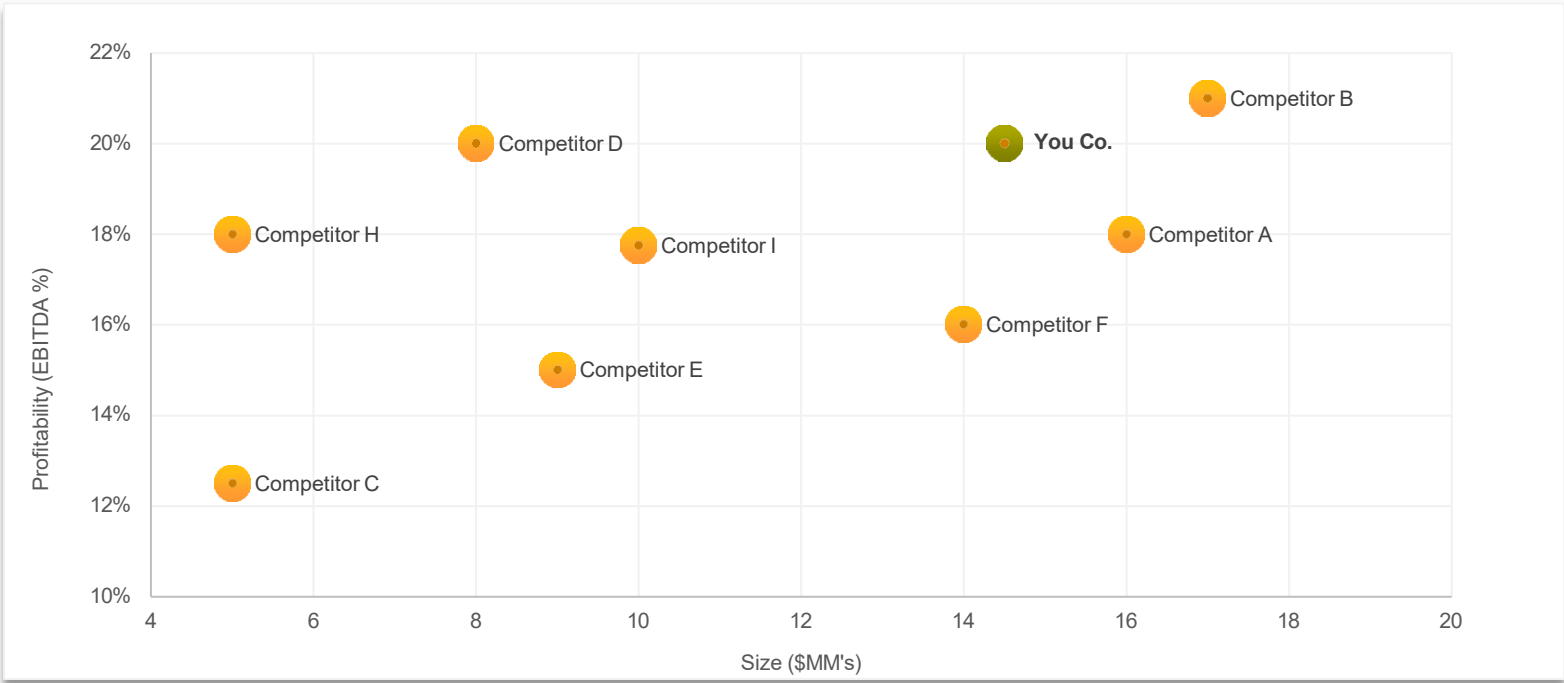


EBITDA Growth YOY



Profitability x Size: You vs. Competition

Where competitors are other anonymized sellers within same product category



IT'S ALL ABOUT DRIVERS

Value Drivers & Other Important Items

Value Drivers

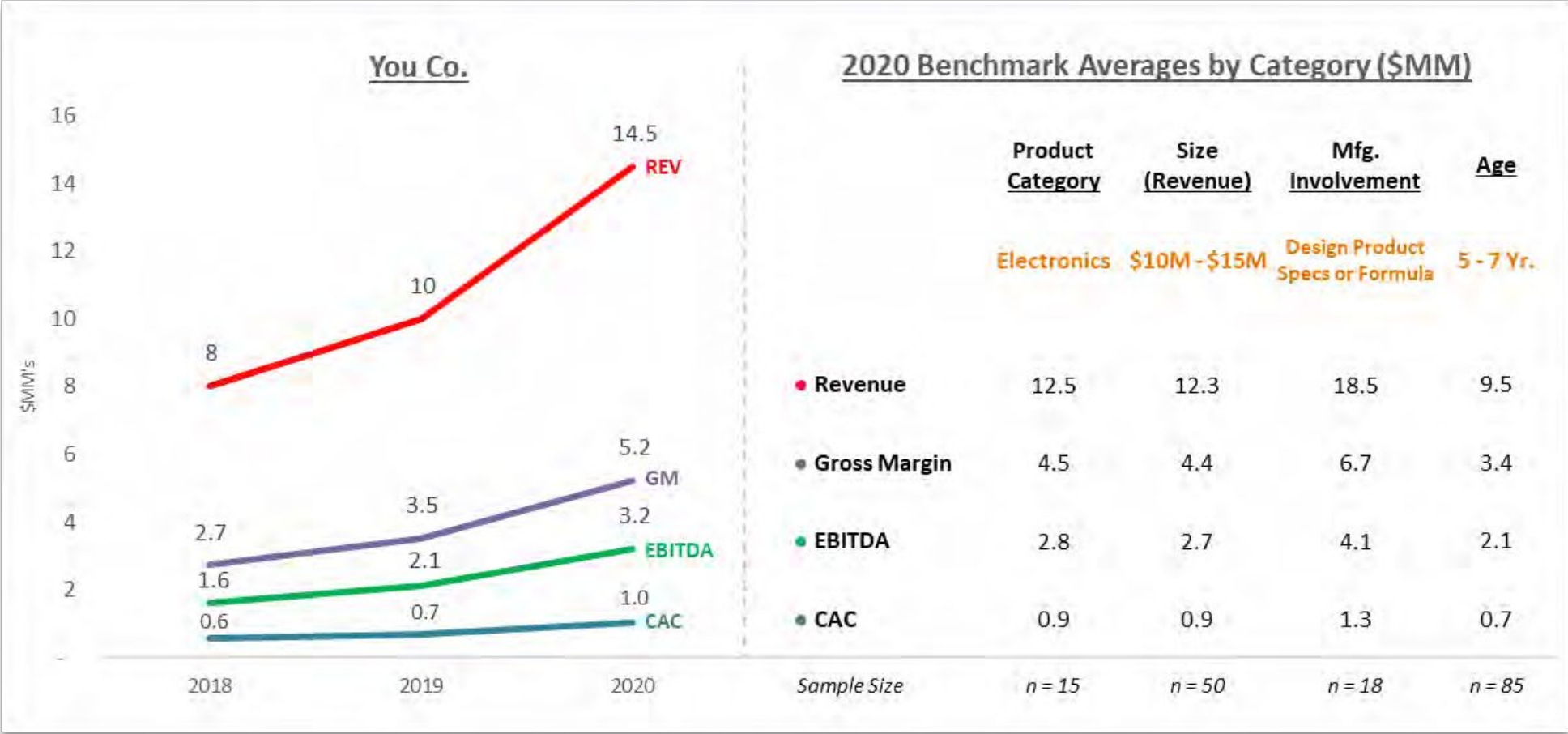
- Competent, autonomous management teams
- Contracts in place with key customers and suppliers
- Key employees covered under non-compete agreement
- Proven track record of revenue and profit growth
 - Buyers don't like to pay for the value they create
- Clean and comprehensive books and records
- Assets are in good operating condition

Other Important Items

- Valuation should be performed very early in the process
- Valuation should only include the assets intended to be sold
- Strategic buyers often pay a premium over financial buyers

ENTITY VALUE DRIVERS

Trended Value Drivers vs. Comparable Peers – Annual Total



VALUATION & GROWTH POTENTIAL

Multiple-Driven Valuation

Est. valuation based on benchmark multiples from peers with shared company characteristics.

Compares against peers within same Product Category, Size, Manufacturing Involvement, and Company Age.

Dollars in \$MM's

	<u>Product Category</u>			<u>Size</u>		<u>Mfg. Involvement</u>		<u>Company Age</u>	
	Electronics			\$10 - \$15		Design Product Specs or Formula		5 - 7 Yr.	
	You	Benchmark	Est. Value	Benchmark	Est. Value	Benchmark	Est. Value	Benchmark	Est. Value
EBITDA	\$ 2.5	5.10	\$ 12.8	4.25	\$ 10.6	3.75	\$ 9.4	3.85	\$ 9.6
Revenue	\$ 4.6	2.80	\$ 12.8	2.33	\$ 10.6	2.06	\$ 9.4	2.11	\$ 9.6

Sample Size:

n = 20

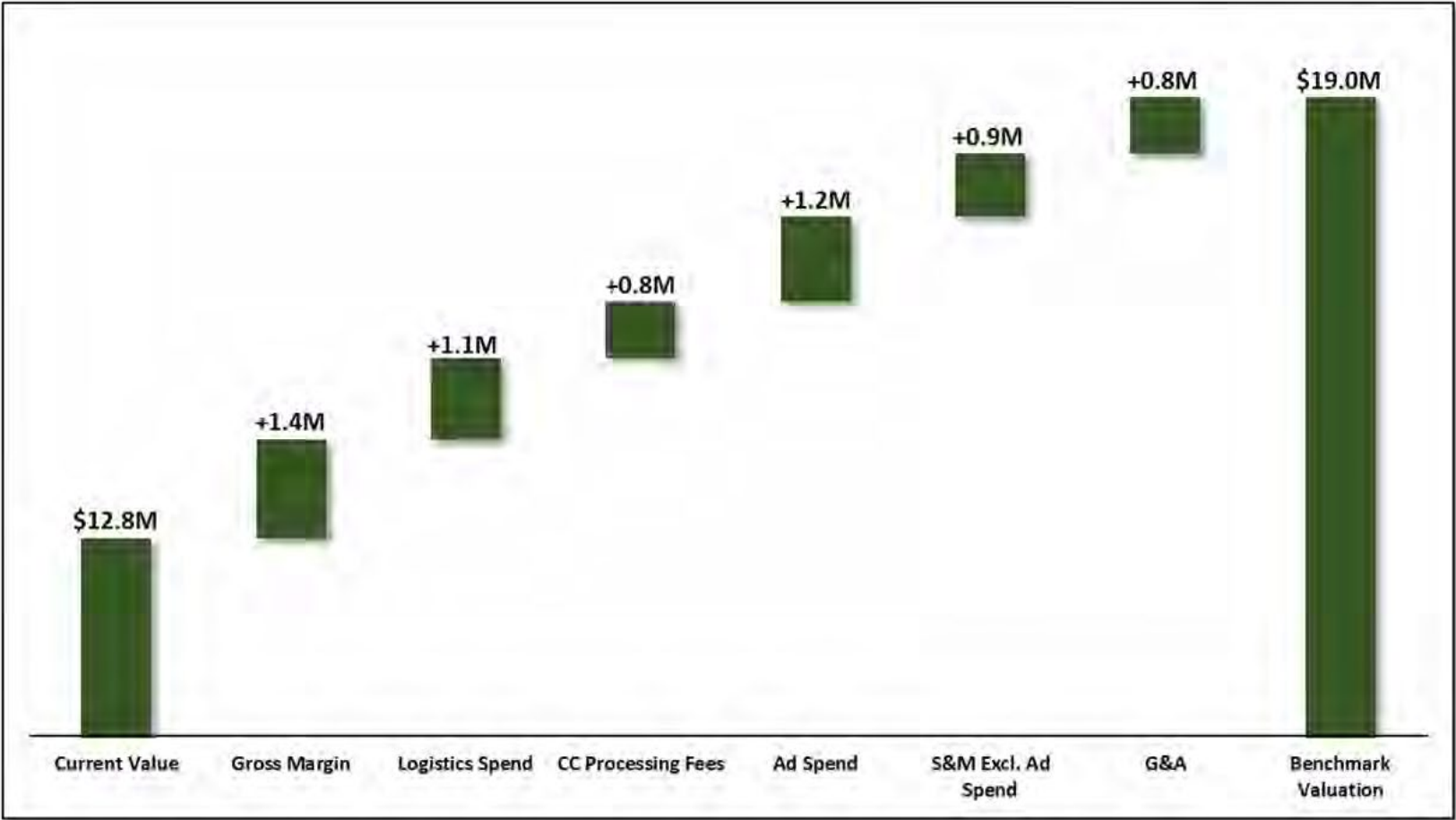
n = 75

n = 10

n = 90

ENTITY VALUATION OPPORTUNITIES

Value-Add Opportunity Waterfall



Increasing the Value of Your Business



PROCESS IMPROVEMENT

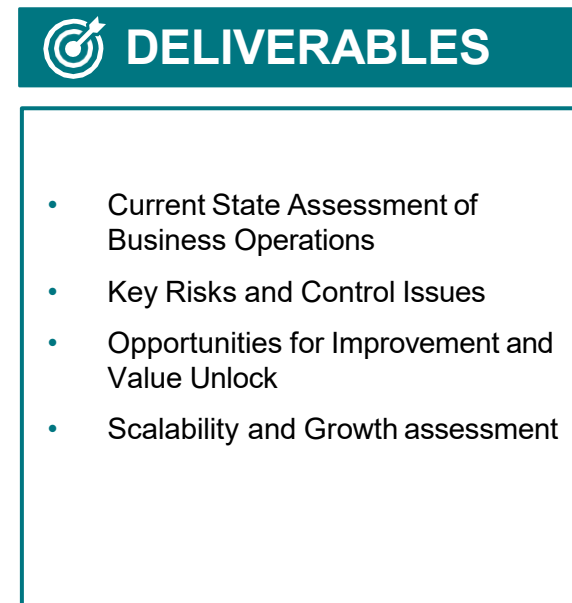
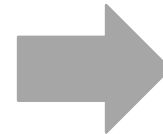
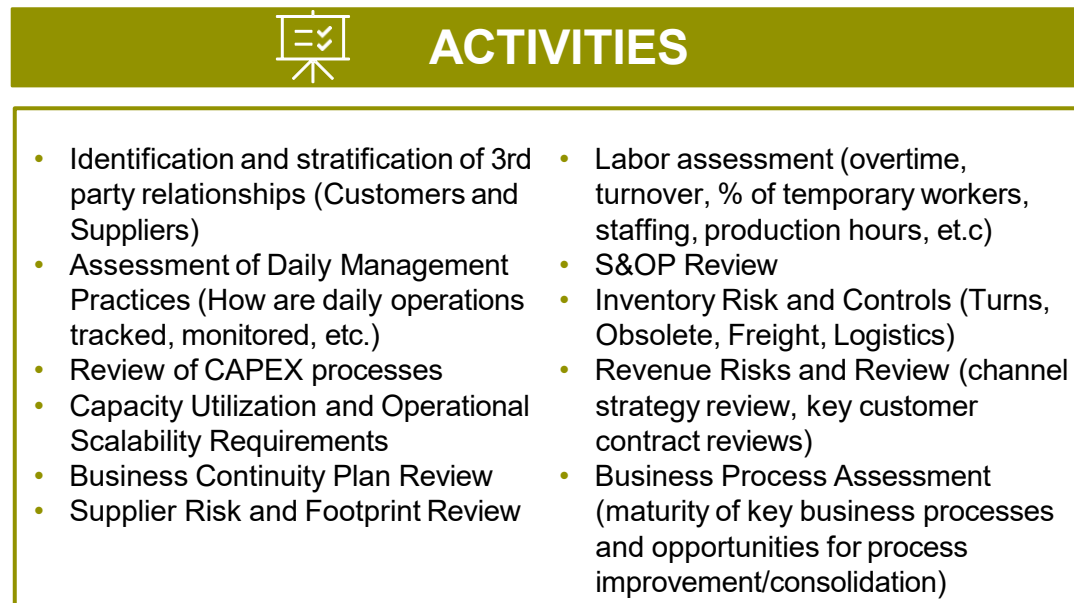
Lean Processes Can Improve Earnings & Enable Growth

Maximizing customer value while **minimizing waste** is the core idea of process improvement. In existing businesses, this is often a transformational journey.

Business Process Improvement

Operational Diligence Preparedness

Operational Due Diligence brings clarity on the current state of operations and the business model of the target company. It may also assess future direction and ability to unlock synergies and/or whether its operational plan can support growth objectives. Finally, it reviews operational and business risks.



AT A GLANCE

We assess:

- Business Risks
- Growth and Opportunities to Scale
- Costs and Supply Chain Footprint Review
- Inventory and Distribution Challenges leading to Liquidity Risks

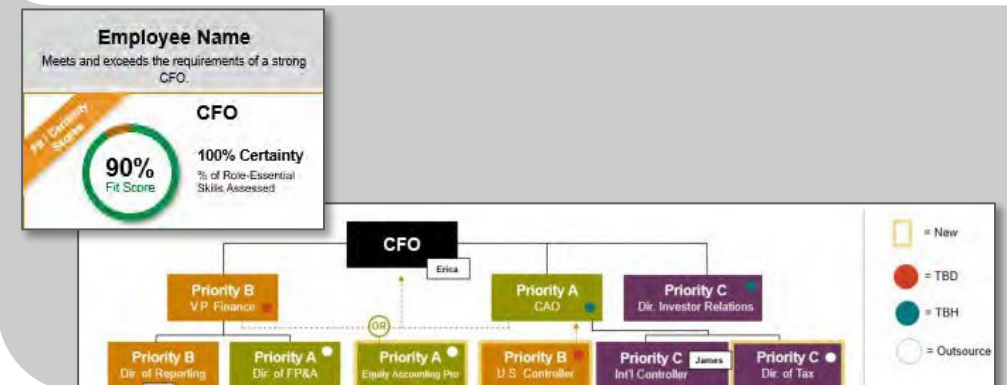
STRATEGY & TRANSFORMATION

Diligence Preparedness of Human Capital Strategy

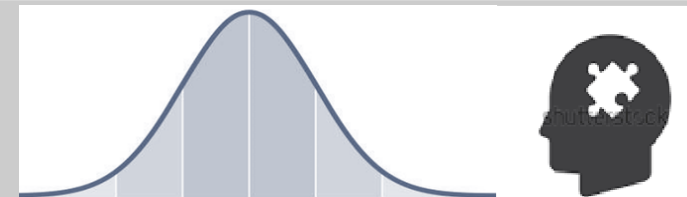
Armanino **evaluates leadership teams** by, holistically providing insight into leadership qualities, and **analytics-based insights on team gaps, strengths, and weaknesses.**

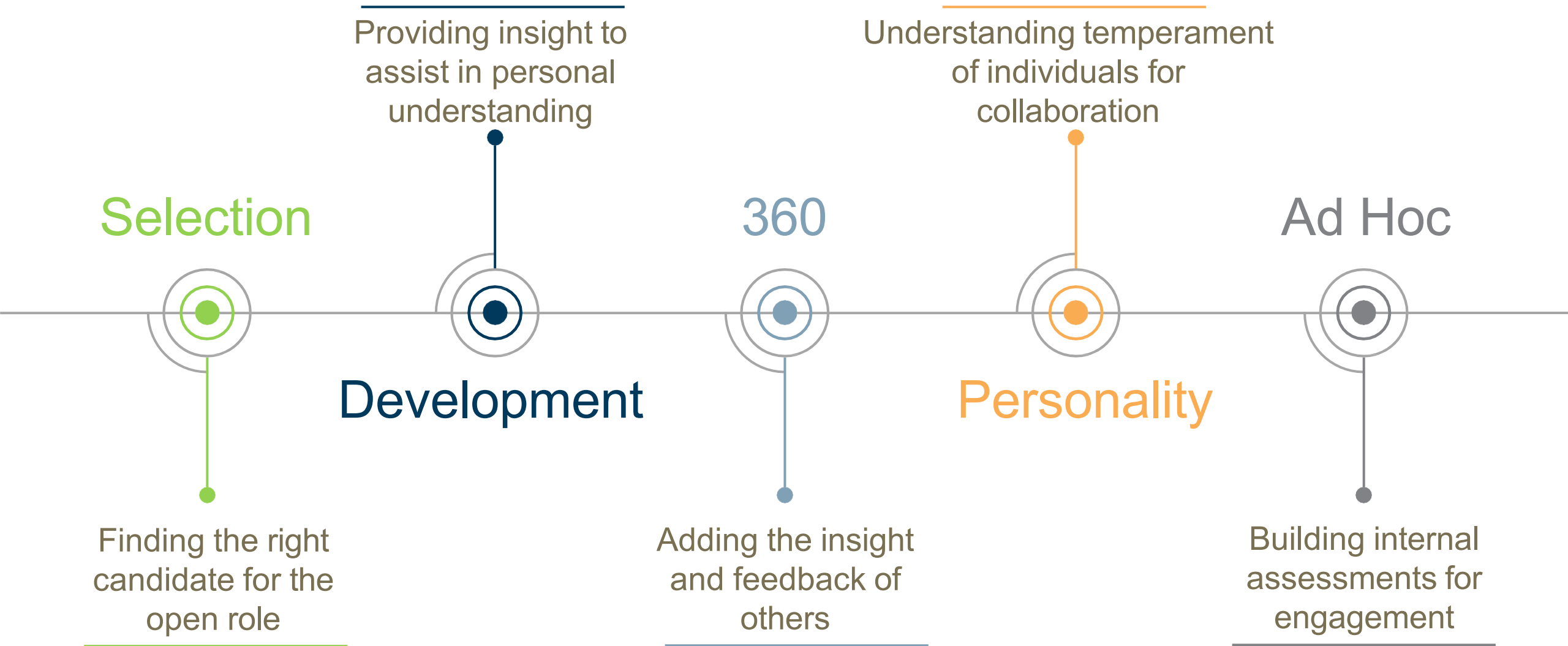


1 IP-Based Leadership Team Evaluation Assessment, Org. Design & Hard Skills Analysis



2 Cultural Insights, Behavioral Profiles, & Executive Coaching





EXECUTIVE LEADERSHIP DEVELOPMENT

PART
1

Understand

- Company
- Team
- Individual
- Goal



PART
2

Coach

- Purpose
- Unison
- Growth
- Result



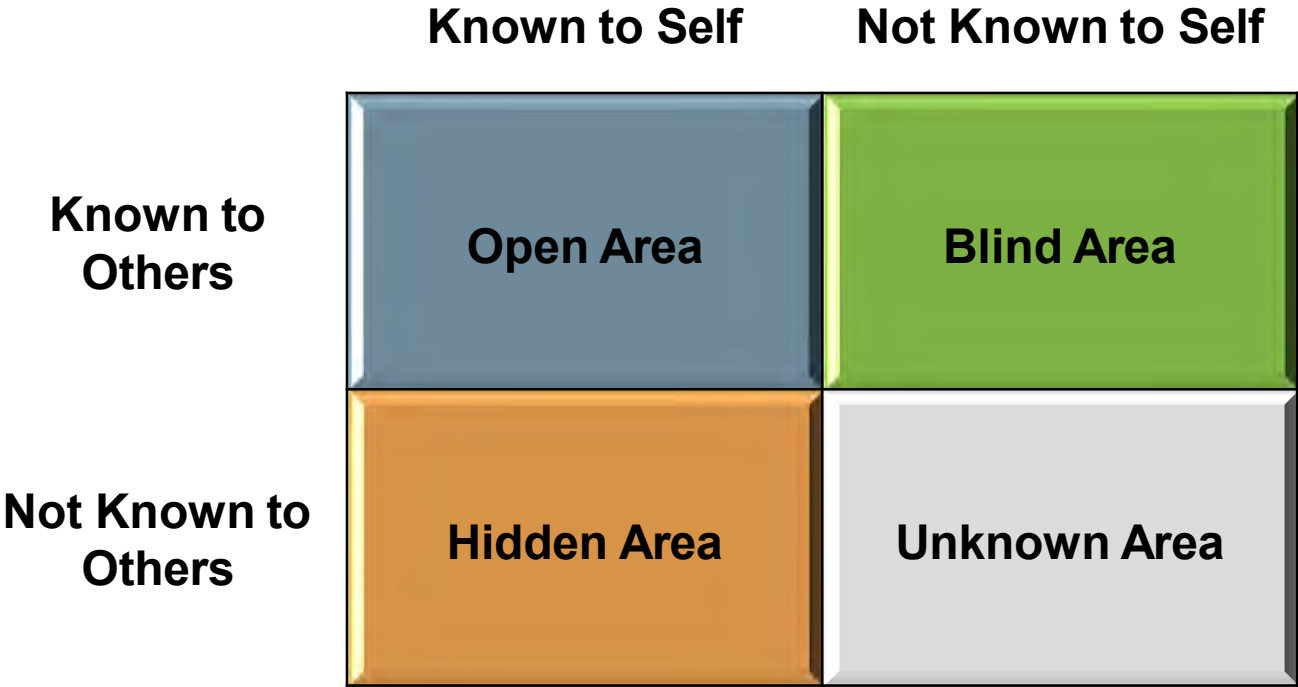
PART
3

Measure

- KPI
- Impact
- Next Step
- Future



Johari Window



DUE DILIGENCE CHALLENGE

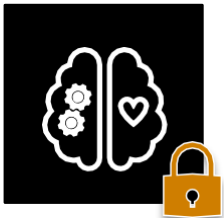
Selecting The “Right” Leaders



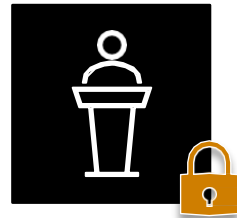
How to accurately assess leaders during the due diligence process...

before the letter of intent is signed?

CULTURE FIT



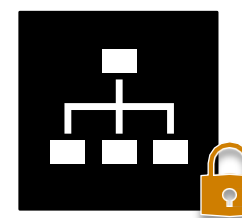
LEADERSHIP STYLES



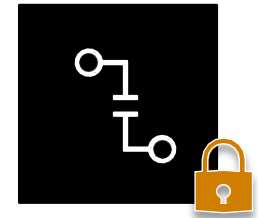
HARD SKILLS



TEAM COMPOSITION



LEADERSHIP GAPS



DON'T FORGET MARKETING

Marketing Strategies to Grow Before, During & After Transition

- How do we assess marketing communications investment and brand value to determine diligence adjustments and add back opportunities?
- What communications strategies and tools should I employ to have a plan pre- and post-sale to engage appropriate internal and external audiences?
- How do we create and control messaging to protect our brand and people during this process?
- How do we ensure a growth mindset during a disruption?

CHANGE MANAGEMENT

Strategic Communications with Internal & External Stakeholders

- Communicate clearly, early, and often
- Communicate through the right people
- Communicate through multiple channels
- Answer the questions, “what’s in it for me?” and “what does it mean to me?”
- Prepare for resistance
- Listen to feedback
- Don’t be afraid to repeat yourself

Preparing for an Exit – The Financials

Polling Question #3

What part of planning for the sale of your business are you most anxious about?

- a) Preparing financial statements
- b) Internal communication
- c) Something else
- d) N/A

THE WHY

Why Prepare Financial Statements for a Sale?

- Financial statements are the key driver of valuation in a sale
- Poor quality financial statements can lead to a lower valuation
- Do you want the buyer to know more about your financials than you do?
- What is the best way to go about preparing your financials?



Having Good Quality Financials won't necessarily increase the value of your business, but having poor financials can negatively impact the value of your business and increase the risk the sale doesn't go through.

THE WHO

Who needs to prepare Seller-Ready Financials?

- Companies with great financial reporting and sophisticated Accounting/Finance
- Companies that have an annual audit performed
- Those divesting a carved-out entity
- Companies with poor financial statements
- Everyone can benefit from preparing their financials for a sale process
- A quality of earnings analysis helps to identify key issues and quantify risks as it relates to the transaction since many issues may not be uncovered until diligence is performed
- It can also identify items that will end up driving value through the process

NOW WHAT?

Process & Preparation Steps

- Getting your accounting in shape
- Applying the tools of finance to improve your performance and boost your value
- Robust, multi-year forward looking forecast model
- Understanding the metrics that matter in your exit
- The sale/partial buyout process itself
- Don't forget about communication!



Quality of Earnings Analysis

\$000s	FY17	LTM Sep-18	YTD Sep-17	YTD Sep-18
Reported Revenue	45,019	45,967	34,633	35,580
Diligence Adjustments				
2 Project Revenue & COGS Recognition	NQ	NQ	NQ	NQ
3 Bill and Hold Adjustment	NQ	NQ	NQ	NQ
Diligence Adjustments (+/- NQ)	-	-	-	-
Diligence Adjusted Revenue (+/- NQ)	45,019	45,967	34,633	35,580
EBITDA Reconciliation				
Net Income	3,873	4,228	3,073	3,428
Depreciation & Amortization	370	432	242	304
Interest Expense	12	19	7	14
Taxes	1	3	1	3
Reported EBITDA	4,257	4,682	3,324	3,749
% of Reported Revenue	9.5%	10.2%	9.6%	10.5%
Management Adjustments				
1 Owner Compensation & Personal Expenses	298	353	209	264
Management Adjustments	298	353	209	264
Management Adjusted EBITDA	4,555	5,036	3,533	4,013
Diligence Adjustments				
1 Owner Compensation & Personal Expenses	(13)	(13)	(10)	(10)
2 Project Revenue & COGS Recognition	NQ	NQ	NQ	NQ
3 Bill and Hold Adjustment	NQ	NQ	NQ	NQ
4 Pro-forma Rent Expense	(37)	(14)	(30)	(7)
5 Transaction Related Expenses	9	20	6	17
6 Business Consulting Expense	18	27	15	24
7 Non-operating Income	(39)	(40)	(14)	(15)
8 Commission Expense Normalization	NQ	NQ	NQ	NQ
9 Employer 401k Match	(140)	(10)	(130)	-
10 Bonus Expense Normalization	(9)	23	(53)	(21)
11 Workers Compensation Normalization	(144)	(81)	(115)	(51)
12 Unrecorded Accruals	NQ	NQ	NQ	NQ
Diligence Adjustments (+/- NQ)	(356)	(88)	(330)	(62)
Diligence Adjusted EBITDA (+/- NQ)	4,199	4,947	3,203	3,951

QUESTION

What is Quality of Earnings?

- Financial accounting analysis of a business to report its recurring rate of earnings.
- Focuses on Earnings Before Interest, Taxes, Depreciation & Amortization, not GAAP earnings.
- Analyzing the sustainability of historical cash flow.

Non-operating Items

- Gain on sale of fixed assets or business
- Owner's personal expenses

Non-recurring or Unusual Items

- Settlement gains
- Site/product line ramp up costs

Accounting Errors

- Missing/double booking of accruals
- Passed audit adjustments

Accounting Policy Changes

- Reserve/accrual methodology changes
- Change in inventory costing

Out-of-period Adjustments

- True ups of prior period accounting estimates
- Out of period gains/losses (reserve builds/reversals)

Non-cash

- Equity compensation
- Asset/business impairments

Non-GAAP

- Cash to accrual conversion
- Improper revenue recognition

NET WORKING CAPITAL

The Overriding Concept

Net Working Capital (“NWC”) represents the amount of cash needed to run a business at a normal operating level throughout the year.

Rationale for Net Working Capital Adjustment

Protection for Buyer and Seller for the economic impact of movements in working capital between signing and closing. Without an adjustment mechanism, Seller may be able to manipulate the closing working capital to increase the “effective” purchase price

Adjustment Mechanism

- Working capital adjustment = Actual working capital at Closing less Target working capital (“normal” level as agreed in the SPA)
- Working capital (i.e., components and methods of computation) and Target (or “Peg”) need to be defined in the SPA
- Unlike the Net Debt Adjustment, the Working Capital adjustment may not be a \$ for \$ adjustment (e.g., working capital collars, offset risk within account movements)



Tax Implications of an Exit

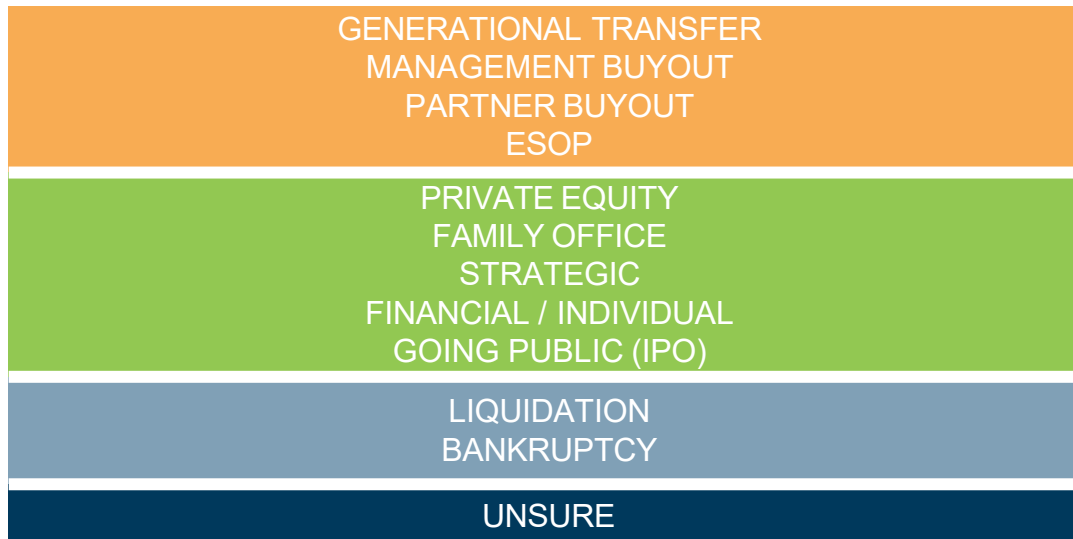
Polling Question #4

Would you like to connect with someone from Armanino regarding preparing for an exit?

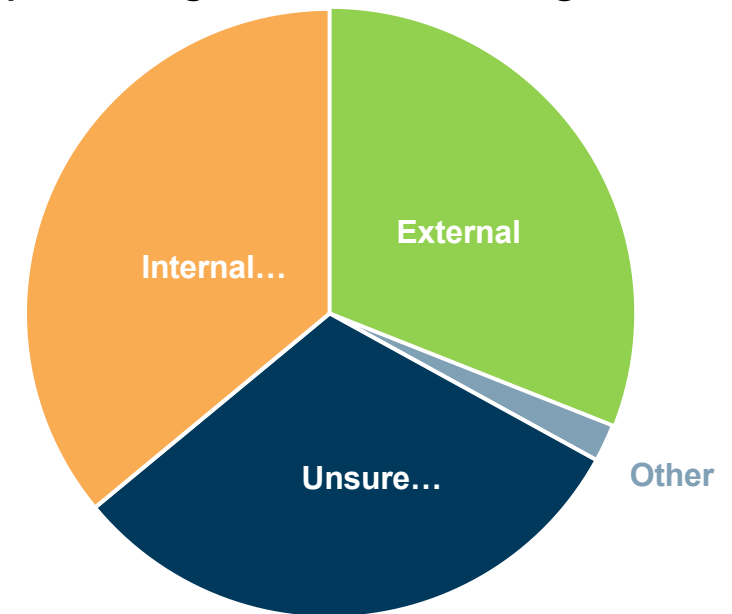
- a) Yes
- b) No
- c) N/A

REVIEW YOUR OPTIONS

Exit Options Analysis

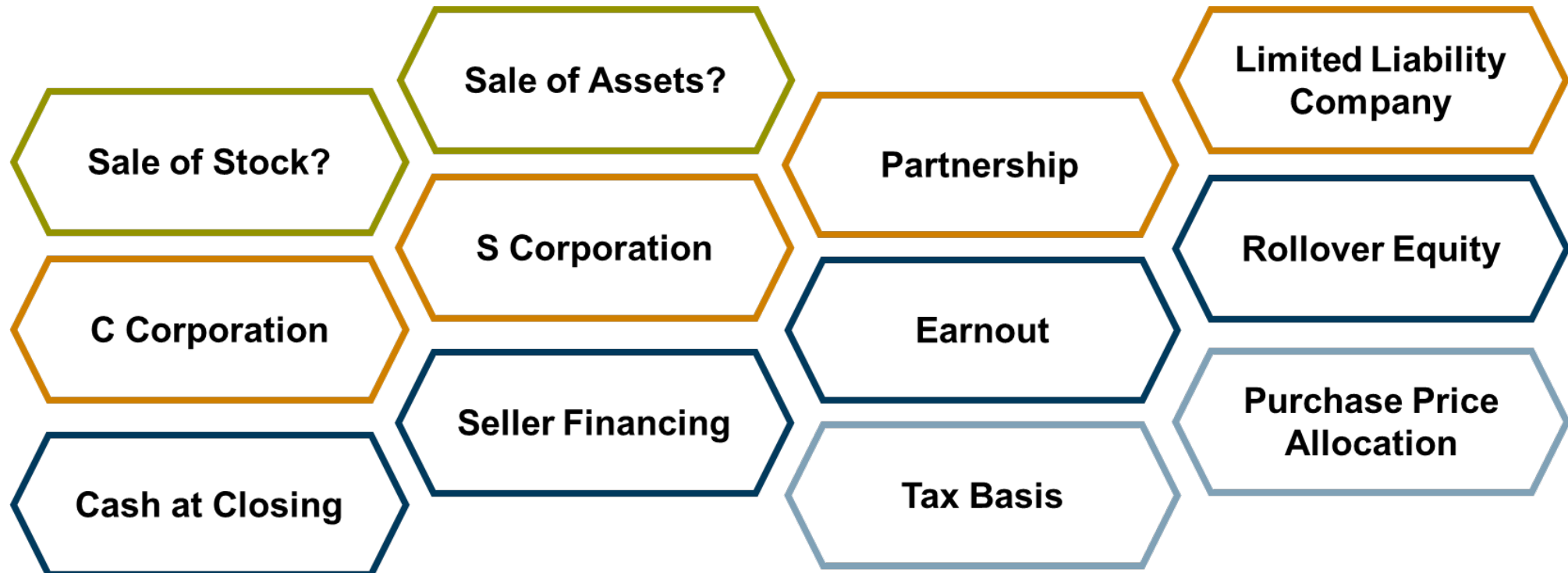


“What best describes how you are planning on transitioning?”



CONSIDER THIS

Deal Structure & Entity Type



Installment Sale

- Seller can defer overall gain and buyer can defer cash outlay
- Risky with the potential increase in cap gains rates, but seller can elect out

Pre-Sale Estate Planning if Goal is to Move some Value of the Business to Future Generations

- It may be more tax efficient to transfer assets before sale
- Transfers or sales to IDGT – Intentionally Defective Grantor Trusts

Post-Sale Ideas/Issues

- Opportunity Zones
- Protect your Proceeds
 - Review your liability protection
 - Diversify your holdings

POST DEAL

After-Tax Cash Proceeds

A tax "waterfall" estimates the seller's net cash after payment of taxes, transaction fees, and debt.

The purpose of this exercise is to educate the seller on how purchase price compares to net cash.

	Asset Sale Scenarios		Stock Sale Scenarios	
	Purchase Price	Purchase Price	Purchase Price	Purchase Price
	\$45,000,000	\$80,000,000	\$45,000,000	\$80,000,000
Gross Cash Proceeds	\$ 45,000,000	\$ 80,000,000	\$ 45,000,000	\$ 80,000,000
Debt Paydown	(29,257,040)	(29,257,040)	(29,257,040)	(29,257,040)
Unpaid Transaction Fees @ Closing				
IB Success Fee	(900,000)	(2,350,000)	(900,000)	(2,350,000)
Advisor Fees	(240,000)	(240,000)	(240,000)	(240,000)
Executive Bonuses	(730,148)	(2,407,648)	(730,148)	(2,407,648)
Before Tax Proceeds	13,872,812	45,745,312	13,872,812	45,745,312
Taxes				
Federal Ordinary Income Tax from Sale	(1,561,300)	(1,135,699)	-	-
Incremental Medicare Tax from Sale	(59,883)	(43,579)	-	-
Federal Capital Gain Tax from Sale	3,000	(6,560,805)	(994,629)	(7,369,129)
Pirmary State Tax from Sale	(279,910)	(2,196,574)	(296,349)	(2,208,699)
Incremental State Tax from Sale	(15,947)	(125,144)	(16,884)	(125,835)
Tax from Continuing Operations	(3,065,198)	(3,065,198)	(3,065,198)	(3,065,198)
Estimated Tax Payments	615,000	615,000	615,000	615,000
After-Tax Proceeds	\$ (4,364,239)	\$ (12,511,999)	\$ (3,758,060)	\$ (12,153,861)
<i>ETR</i>	36.7%	28.9%	32.2%	28.1%
Seller net cash	\$ 9,508,573	\$ 33,233,313	\$ 10,114,752	\$ 33,591,451

Q&A

Thank you for
attending

Additional Questions?

Reach out to us at

Experts@armaninio.com





FUTURE CONTENT

Stay Tuned!

1. Process & Systems (Tech Stack) Improvements to Increase the Value of Your Business
2. Preparing Your Financials for the Sale Process
3. Preserving Your Wealth - Tax Estate Planning Considerations

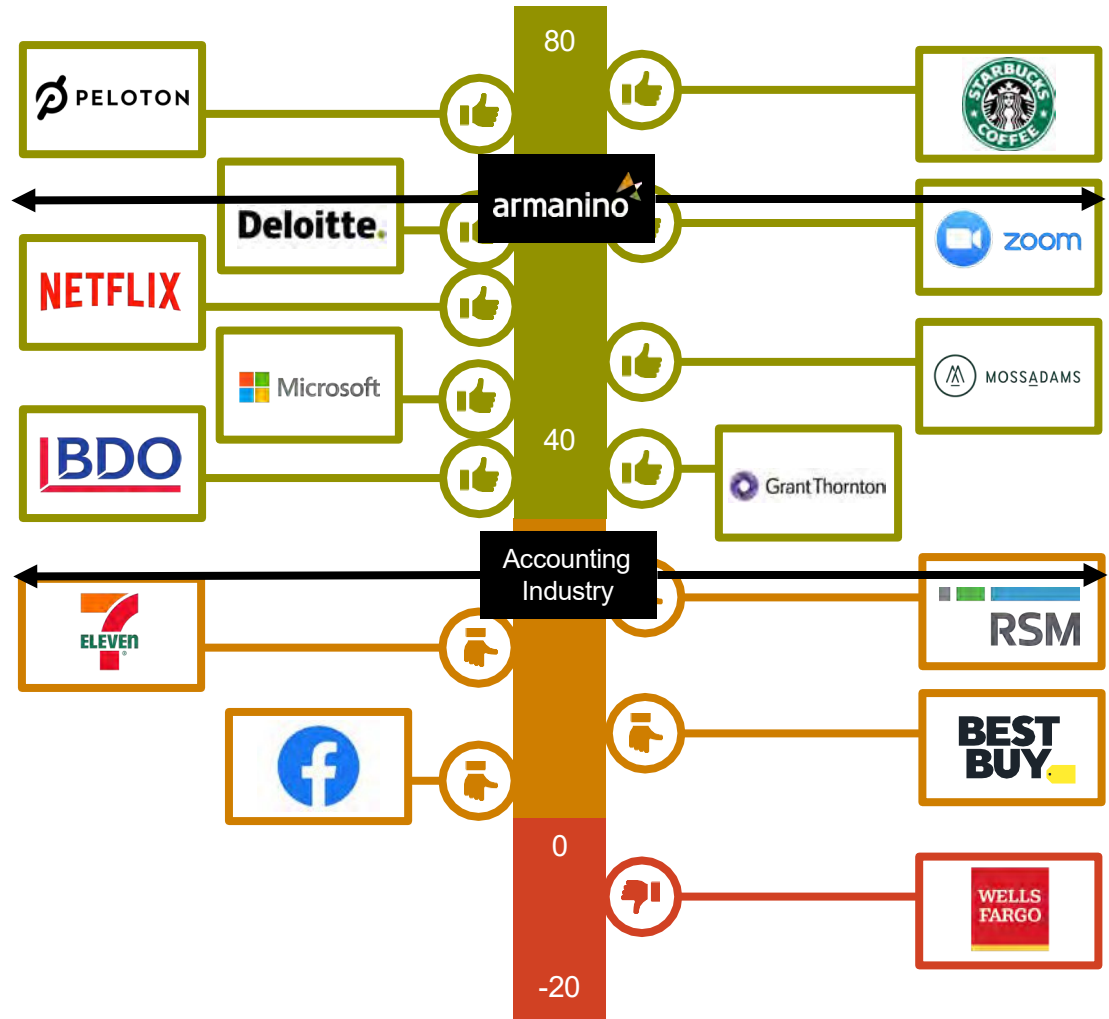
... And more!

OUR CLIENTS' VIEW

We Know You'll Love Us

A Net Promoter® Score (NPS) is used by more than two-thirds of Fortune 1000 companies.

Armanino's NPS (68) is almost two times higher than the accounting industry average (38), and it places the firm scores closest to household name brands such as Starbucks, Peloton and Zoom.



Armanino offers **clarity** in a disruptive, ever-evolving world

Equipping you with the insights and tools needed to succeed today, and in the future



COMPLIANCE & REGULATORY

- Tax Planning
- Trust & Estate
- SOX
- Contract



ASSURANCE & ADVISORY

- Cybersecurity
- SOC
- Restructuring
- Revenue Recognition



STRATEGY & PLANNING

- Corporate Strategy
- Strategic Advisory
- Benchmarking
- Business Transformation



STAFFING & DEVELOPMENT

- Payroll
- Health Benefits
- Executive Search
- Interim Placement



TECHNOLOGY SYSTEMS

- ERP
- CRM
- Business Intelligence
- Managed Services



ACCOUNTING & BACKOFFICE

- Bookkeeping
- Budgeting/Forecasting
- Account Receivable
- Accounts Payable



Possible *(Re)*Defined™

Armanino is a brand name used by Armanino LLP, Armanino CPA LLP, and Armanino Advisory LLC, independently owned entities, to provide professional services in an alternative practice structure in accordance with law, regulations, and professional standards. Armanino LLP and Armanino CPA LLP are licensed independent CPA firms that provide attest services, and Armanino Advisory LLC and its subsidiary entities provide tax, advisory, and business consulting services. Armanino Advisory LLC and its subsidiary entities are not licensed CPA firms.