THE OVERLOOKED OWNER:

A Key Factor in Determining Business Value

The ValueBuilder System™

Double Your Value. Double Your Offers. Control Your Future.

FOREWORD

We widely accept that determining the value of a business is a scientific process. Most people think that determining the value of a business involves an in-depth look at the books, sizing up the market, and many other types of quantitative analysis. It is also common to evaluate the management team and their skills and track record.

The most overlooked aspects of determining business value are often the owner and their intentions, specifically, the number of owners, the reasons for exit, and the steps taken to prepare the business for exit. Based on our analysis of 1,511 business owners and their companies, the owner's personal reason for exit and the actions they have personally taken to exit play a significant role in the value of their business.

When comparing two similar businesses in the same geography and industry and of a similar size, if each owner has different reasons for exiting, they will likely have drastically different business values. Other factors that can impact the value of the business include the owner's steps to prepare for exit and the proportion of shares owned. When added up, these factors can predict up to 53% of the difference in the value of two seemingly similar businesses.

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PART ONE:

OWNER'S REASONS FOR EXIT

One hundred percent of business owners exit their businesses—either by design or by default. We can bucket these reasons into three categories that play a role in the value of the business.

1. PERSONAL MOTIVATORS

The first category is personal motivators. The exit reasons include:

"Looking to diversify my wealth."

"I want to cash out."

"I have a new business I want to start."

"I'd like to get involved in philanthropy."

When the owner is personally motivated to move on to a new project or chapter of their lives, the value of the business is higher. One might conclude that this category of owners has met the goals they set out for themselves and the business and are motivated to exit to move to the next phase of their lives.

2. PERSONAL CRISIS

The second category is a personal crisis. The exit reasons include:

"I'm burned out."

"I have health issues."

"I am stressed and time-starved."

"I have a family crisis."

It appears that when the owner is experiencing a personal crisis, they are negatively impacting the value of the business. The owner may be operating ineffectively due to their circumstance and is failing to meet their personal and business goals. They may be focused on trying to survive rather than harvesting the value of the business.

Included in this category is the reason "Time to retire." This response negatively impacts the business's value slightly but less than an owner's personal crisis does. One might conclude that the owner desires to retire because they have met their personal goals but the business has not met the envisioned goals. The owner is hanging up the towel and is not focused on preparing for the exit.

3. PERSONALLY PEAKED

The last category is personally peaked. The exit reasons include:

"I'm just bored."

"I want to spend time on a hobby."

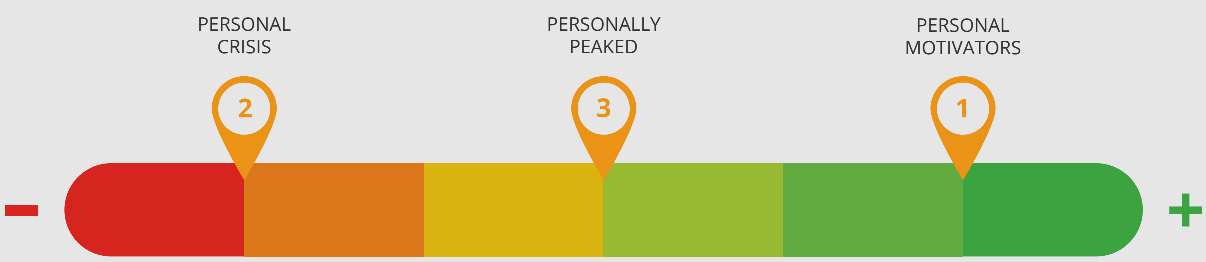
"I want to travel."

"I want to focus on my health."

It appears that when the owner feels they have peaked personally, their reasons for exit do not impact the value of the business.

PART ONE:
IN SUMMARY

Of the three reasons to exit, it appears that Personal Motivators will have the most positive impact on business value. In contrast, a Personal Crisis will have the most negative effect. Lastly, if the exit reason is Personally and Professionally Peaked, our research suggests no impact on business value.



RELATIONSHIP WITH BUSINESS VALUE

PART TWO:
PREPARING FOR EXIT

The decision to exit is only the first step in a series of critical decisions an owner must make. How an owner prepares themselves and the business for exit also plays an important role in determining company value. We analyzed the following areas of an owner's preparation to exit: an owner's personal financial goals, personal life and social goals, involvement after exit, employees' well being, and ownership structure. How an owner approaches each of these five areas will have an impact on company value.

1. PERSONAL FINANCIAL GOALS

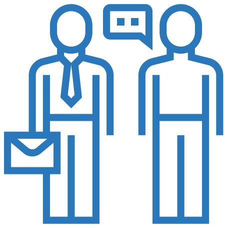
Many business owners talk about their business like it's one of their children—maybe even their favorite one. Ask virtually all parents, and they will state that they can't assign value to their children. Similarly, some owners believe their business is invaluable and think of the highest number they will get offered for the business rather than the lowest they are likely to accept. We define a "minimum number" as the lowest number a business owner will accept to exit the company with no future regrets. Owners who have thought about their minimum number build a business that is 5-6% more valuable.

Interestingly, the owner does not have to verify if their minimum number is accurate to have a more valuable business. The simple act of thinking about the number appears to help the owner prepare for the exit and to have a more valuable company.

2. PERSONAL LIFE AND SOCIAL GOALS

Just like parents raising their child, some owners invest all their time into their business, sometimes spending upwards of 60 hours a week working in their company. They become friends with their employees, inviting them into their homes and to milestone celebrations like their children's weddings. Business owners who are aware of how the exit will impact their social circle appear to have a slightly more valuable business.

3. INVOLVEMENT AFTER EXIT



Many owners think that the exit will be simple. Like selling a house, they will hand over the keys and get a bag of cash in return. Exiting a business is very different from selling a house. The more an owner is willing to remain involved in the business after exit, the more valuable the company appears to be. An owner who is willing to accept any option beyond handing over the business and walking away will have a 4-5% more valuable business. There seems to be a premium paid by the buyer for an owner to stay involved through the transition process.

4. EMPLOYEES' WELL BEING

Parents holding their newborns often wonder about their baby's future life—career, family, and personal goals. They may wonder how their parenting will impact the lives of their children. Similarly, some business owners wonder how the buyer will treat their employees after they exit. Some owners may plan how they will thank their employees, while others will take steps to negotiate with the buyer to look after their employees. Having a plan and thinking through the employees' well being appears to lead to between a 17-21% increase in business value, regardless of if they have shared their exit plans with their employees.

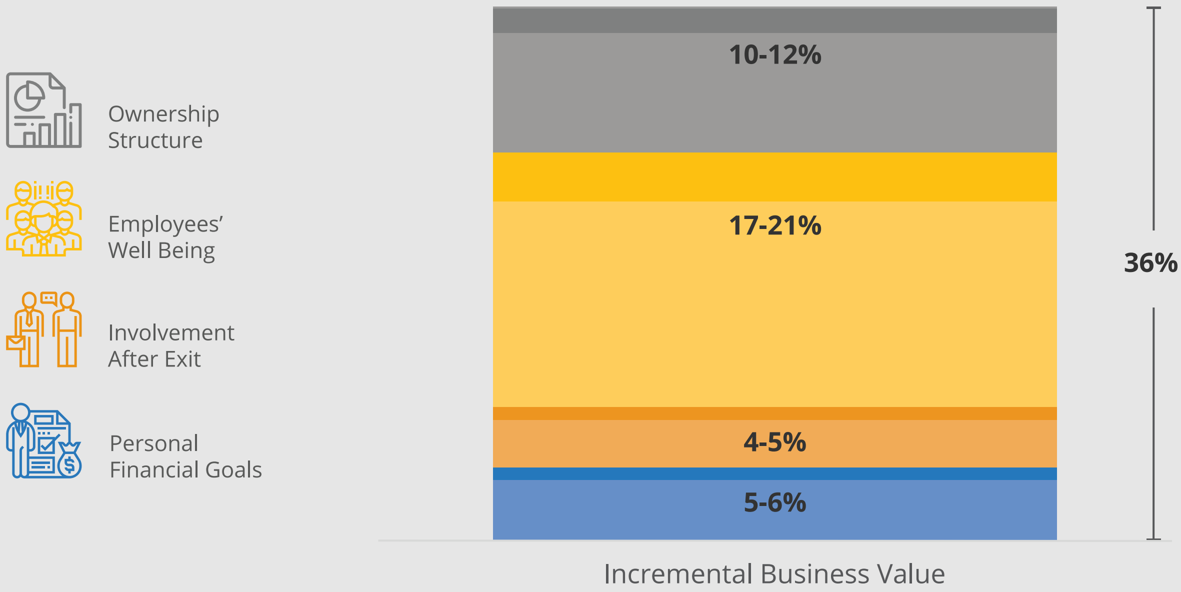
5. OWNERSHIP STRUCTURE

The fewer shares the majority owner holds, the more valuable the business is. Businesses with more than one owner appear to be 6% more valuable. The value of the company appears to be 10-12% higher when there is no shareholder that owns 50% or more of the business. There could be many reasons for a higher value when there are multiple owners. One might conclude that business owners that control 100% of the company are accountable only to themselves, while multiple owners are accountable to one another. Alternatively, with more opinions freely expressed when deciding the future of the company, the better the business operations and the higher the value. More research would have to be done to understand this relationship and is out of the scope of this paper.

PART TWO:

IN SUMMARY

As business owners prepare for exit, how they approach these four areas can drastically impact business value. If all four areas are addressed effectively, owners can expect a 36% increase in the value of their business.



TAKING ACTION

While a business owner may never know when a personal crisis will strike, they should always be ready to exit. Here are four suggestions that any business owner can start today, regardless of when they are looking to exit, whether 5, 10, or 20 years from now. You might want to take an annual day of reflection to consider the following:

1. CONSIDER YOUR NEXT CHAPTER

Take some time to figure out the next phase of your life. For example, if you want some time to travel and relax before starting a new chapter, you may want to have a project always lined up. This can help remind you that the current business is only a chapter in your life. Here are some questions to get you started:

- ***What will your professional life entail? Will it include starting another business, consulting, investing, retiring, or something else?***
- ***What will you do in your next chapter to give your life a sense of purpose?***
- ***What kind of lifestyle do you aspire to have?***
- ***What relationships will you invest more in?***
- ***What hobbies and interests will you indulge in?***

2. KNOW A MINIMUM NUMBER

While you may not know the value of your business, you should consider having a minimum number. This is the minimum amount of money you want to garner from selling the shares of your business to be able to look back on your exit without regret. Knowing this number alone can help you realize a more lucrative exit.

3. IMAGINE YOUR EXIT

It's fun to imagine the day you ultimately exit as dropping off the keys and riding into the sunset. Realistically, that may not happen. Contemplate what possible roles you would be happy to continue working in within the business, in what capacity, and for how long.

- ***Are you willing to stay on as a consultant?***
- ***Will you assume a minority ownership role?***
- ***Do you prefer to stay on as an operator with a majority role?***

Answering these questions on an annual basis can maximize the number of options to exit and the amount you garner.

4. THINK ABOUT YOUR EMPLOYEES

Think of all the employees that have helped you make your business a success. Consider how you want the buyer to treat them. One exercise is to make a list of all your key employees.

- ***Beside each name, check off if you want to include them in helping you get the business ready for exit.***
- ***Determine how you want to thank that employee for helping you achieve your exit. It could be through employee stock options or a monetary amount.***
- ***Decide how and when you will tell them about your decision to exit.***
- ***Decide whether their future employment is necessary to include in your exit plan.***

Spending some time thinking about your exit, the next chapter of your life, your minimum number, and your company's succession can help you maximize the value of your business.

CONCLUSION

It's popular to think of business valuation as an exact science. However, an owner's readiness to exit appears to play a significant role in the overall value of their business. While an owner may not know when they might have to exit a business due to a personal crisis, being prepared to exit can pay off when it's time. To do this, an owner can start by considering life after the exit for both themselves and the business. Every owner wants to maximize their business value, and they must understand how their personal readiness can impact it.