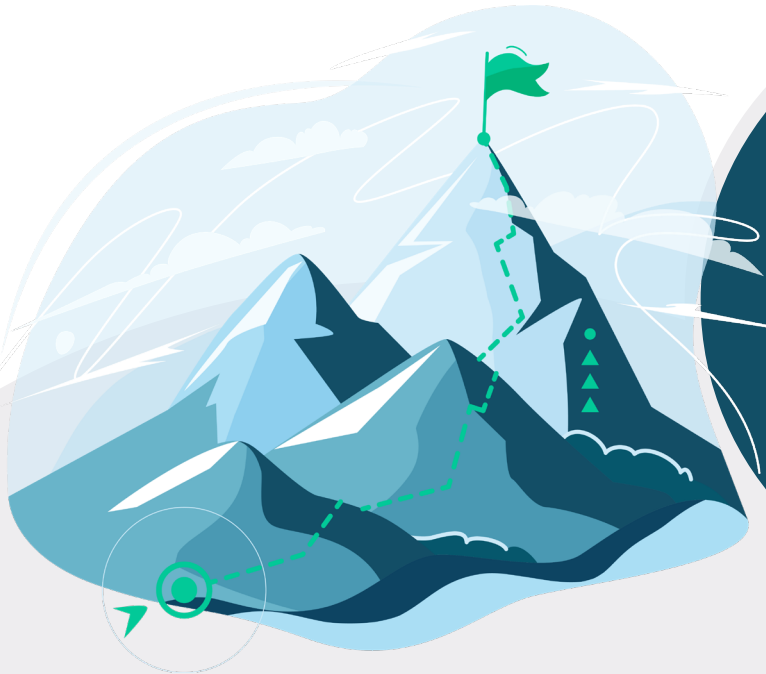
PITFALLS OF SELLING YOUR BUSINESS WITHOUT A PLAN

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Running a business is hard. Selling a business is potentially harder. We recently partnered with a business owner (let's call him Fred) to help him transition his business. Fred's business is now sold, and the money transferred. There is celebration in the air, and we are all excited for Fred and his family to start the next chapter.

However, we can't help but reflect on what it took to get here and the lessons we learned along the way. The decision to sell a business can be a significant milestone for entrepreneurs, requiring careful planning to avoid the pitfalls that can be associated with such a complex process. In the following paragraphs, we'll dig deeper into the challenges associated with selling a business without a comprehensive exit plan, emphasizing the critical issues of owner centralization, income replacement, and the often-overlooked dilemma of owners not understanding their exit options and where to seek the right advice.

Fred experienced most of these challenges along the way, and in an effort to save other owners from the same pain, we are sharing the top pitfalls here:



> "Running a business is hard. Selling a business is **POTENTIALLY HARDER.**

#1– The Knowledge Gap: Exit Options and Expert Guidance

One of the primary pitfalls business owners face is a lack of understanding about their exit options and the absence of knowledge regarding where to seek the right advice. It's easy to look at a similar business and say, "That looked easy – I want that payout, too." But what worked for one owner might not work for another. This knowledge gap can lead to a variety of issues, including:

- **Limited Exploration of Exit Paths:** The lack of awareness about various exit options may result in owners overlooking potentially beneficial strategies. From mergers and acquisitions to employee stock ownership plans (ESOPs) or family transfers, each option comes with unique advantages and challenges that must align with the owner's goals.
- **Inadequate Professional Guidance:** Without a clear understanding of where to find the right advice, owners may engage with professionals who lack the expertise necessary for a successful business sale. The absence of professional guidance can contribute to suboptimal decision-making and unsatisfactory outcomes.
- **Unrealistic Expectations:** Owners may harbor unrealistic expectations about the sale process due to a lack of professional guidance. Fred certainly experienced this one. Four offers fell through over the course of five years. Unrealistic timelines, valuations, and potential challenges can lead to disappointment and frustration during the sale process.

To mitigate these pitfalls, business owners must actively seek out a team of professionals, such as business brokers, financial advisors, and legal experts who specialize in structuring business exits. If Fred had engaged with these experts earlier on, we suspect the business sale would have gone through in half the time. This isn't because his first team wasn't talented—it's because the right team knows how to say "yes" or "no" faster. And in Fred's case, he should have said "no" to the first three offers much faster. Early engagement of a team can provide owners with a clearer understanding of their options, realistic expectations, and the expertise needed to navigate the complexities of a business sale successfully while the owner focuses on the business.

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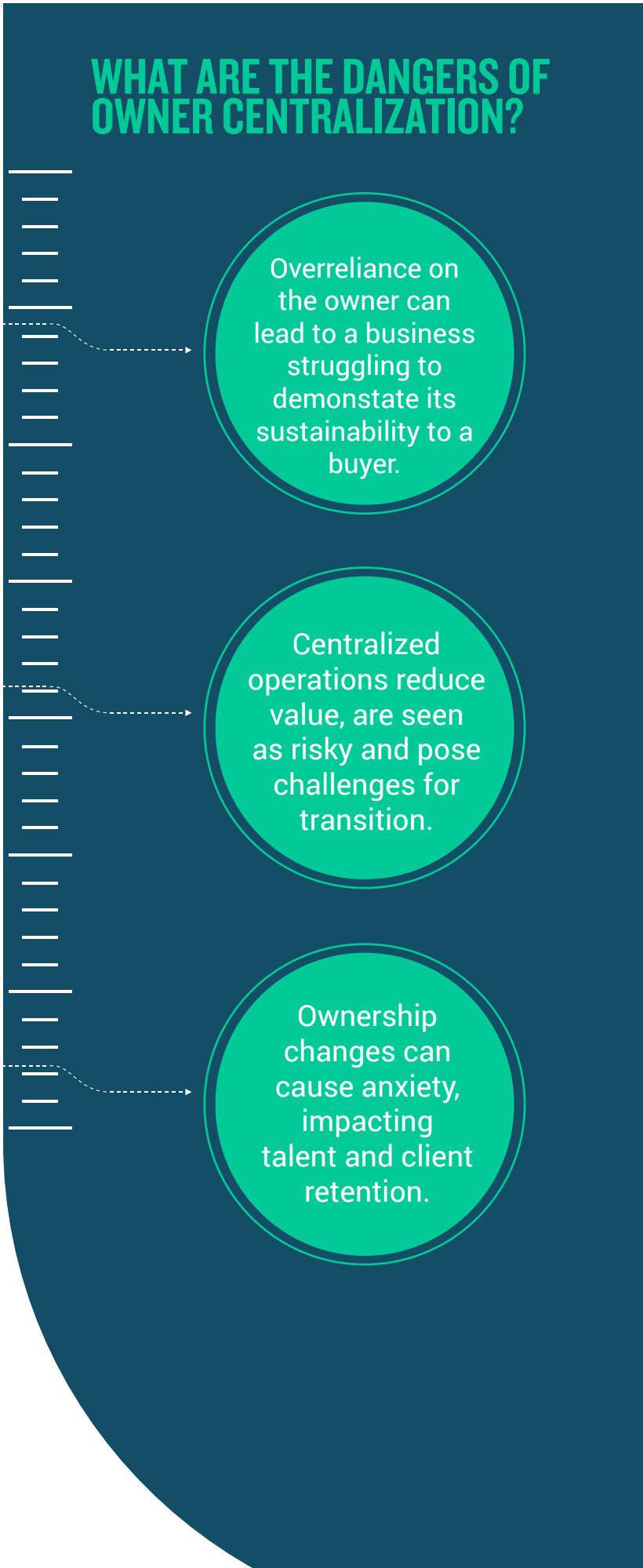
#2 – The Dangers of Owner Centralization

Owner centralization poses a significant challenge for business owners looking to sell. Fred was no exception. The business was him and he was the business. That, plus specific licenses that he held to operate the business, made it even harder to sell. Fred's story isn't unique in this way.

Most small business owners struggle to scale the business beyond themselves. The pitfalls associated with owner centralization include:

- **Overreliance on the Owner:** This occurs when decision-making and operational responsibilities are overly concentrated, typically with the owner or within a select group of executives. A business that is dependent on the owner's involvement and expertise may struggle to demonstrate its sustainability to potential buyers.
- **Reduced Perceived Value:** A centralized business may be perceived as high risk by potential buyers, affecting its valuation. The lack of a diversified management structure and documented processes can make it challenging for new owners to envision a smooth transition.
- **Employee and Customer Concerns:** Sudden changes in ownership can lead to anxiety among employees and customers if the business relies heavily on the owner's relationships. This can result in a loss of key talent and clients during the transition, directly impacting the business's value.

Mitigating the dangers of centralization requires a proactive approach to building a strong management team, documenting processes, and ensuring the business is not overly reliant on the owner's direct involvement. This shift towards decentralization not only enhances the perceived value of the business but also positions it for a smoother transition.



#3 – Maximizing Transferable Business Value

A key goal in exit planning is maximizing the transferable value of the business. When Fred first considered selling his business, most of the processes and systems lived in his head. That made it very difficult for potential buyers to understand the business they were buying. Ironically, he had to put the infrastructure in place at the end of the life of the business. We could only imagine what would have happened to the enterprise value if he had done this earlier. But as they say, "Better late than never." To truly impact the transferable value (hopefully earlier than Fred did), you'll want to take a multifaceted approach that addresses several critical factors:

Diversification of Business Value:

Owners need to ensure that their business's value is not overly concentrated in specific areas, such as customer relationships or proprietary technology. A diversified and well-documented value proposition makes the business more attractive to potential buyers.

Building a Strong Management Team:

Developing a robust management team capable of running the business independently is crucial for maintaining or increasing its value post-sale. Buyers seek businesses with a solid foundation that can thrive without the constant involvement of the current owner.

Investing in Infrastructure and Systems:

Owners should invest in the infrastructure and systems necessary for sustained success. This includes technology, processes, and employee training that contribute to the overall efficiency and attractiveness of the business to potential buyers.

By strategically addressing these factors, owners can enhance the overall value of their business, making it more appealing to potential buyers.

#4 – Financial Planning for Post-Sale Income Replacement

Concerns about income replacement post-sale are a common source of anxiety for business owners. Many owners think of their business as their personal ATM, which spits out money as a result of their hard work. When faced with selling the business, they often struggle to understand where and how they'll draw income to live off of. A robust financial plan should address various aspects to ensure financial stability:

- **Determining the Sale Value Needed:** Owners must have a clear understanding of the financial implications of selling their business. This involves calculating the amount needed from the sale to replace the income generated by the business and sustain their desired lifestyle.

- **Exploring Investment Opportunities:** Beyond the sale, owners should explore diverse investment opportunities to ensure a stable and growing income stream. We spent a lot of time with Fred mapping this out. We took the net (after-tax) sale proceeds and designed a portfolio that generated a significant percentage of the income that Fred needed when he no longer had the business ATM. By investing half of the proceeds in income investments (like private loans and other fixed-income strategies) and half oriented towards growth (like real estate or stocks),

we've been able to achieve a nice balance of both providing for his lifestyle and growing his nest egg. A well-rounded portfolio can make all the difference when it comes to owners sleeping at night, knowing they and their family have the financial resources to live a meaningful life.

- **Considering Tax Implications:** Financial planning should also account for tax implications associated with the sale. Minimizing tax liabilities is crucial for maximizing the net proceeds available for income replacement.

By comprehensively addressing these financial considerations, owners can approach the sale with a clearer understanding of their financial needs and a well-defined strategy for maintaining their desired lifestyle post-sale.

#5 – The Comprehensive Exit Plan: A Blueprint for Success

In conclusion, a successful business exit requires a comprehensive plan that goes beyond addressing the pitfalls associated with centralization, income replacement concerns, and knowledge gaps. The overarching goal is to create a blueprint for success that encompasses:

- **Understanding Exit Options:** Owners should educate themselves about the various exit options available, seeking professional advice to align their choice with their unique goals and circumstances.
- **Building a Robust Management Team:** Actively working towards decentralization by building a strong management team and documenting processes to enhance the perceived value of the business by reducing risk.



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can make all the difference when it comes to owners sleeping at night.

- **Maximizing Transferable Business Value:** Strategic efforts to diversify business value, develop a capable management team, and invest in infrastructure and systems to position the business as an attractive proposition for potential buyers.
- **Financial Planning:** A thorough financial plan that calculates the sale value needed, explores investment opportunities, and considers tax implications to ensure a stable and secure financial future.
- **Personal Planning:** Deliberate consideration of personal goals, emotional preparedness, and a vivid vision of what life looks like after the business is sold.

We don't want the lack of a comprehensive exit plan to jeopardize the legacy many business owners have built. If you were to ask Fred for his best advice, he would say, "Take charge of your business destiny early by hiring the best advisory team, getting the 'business house' in order, and building a financial plan that provides a vision for life after the sale."

The time to act is now—your business and your legacy await the next chapter.

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