Who Says You Can Only Sell Your Business Once?

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Ways to Take a Second Bite of the Apple

Picture this: Your business is booming and growth seems inevitable, but you are nearing retirement and want to think about slowing down. You want to sell your business, but you know selling it now would mean you would be leaving money on the table when it hits its profit peak a few years from now. What are your options?

There are a few opportunities owners have when they start considering selling their business that allow them to benefit from the business long after the sale. Some options even allow for the sale to be split up, so the business can be sold by the same owner more than once. Here are three of those options.

Option One - Sell 100% of Your Business, but Include an Incentive Earn-Out in the Sale Terms

An earn-out is an option where the seller finances a portion of the sales price through the earnings of the business. In other words, the buyer will pay a certain percentage of the sales price up front and the rest will be tied to earnings of the business after the transaction. This can be a good option if there is a difference in what the buyer thinks the business is worth and what the owner thinks it is worth. In other words, the owner can obtain additional compensation if the business achieves certain goals after the sale. An example would be the buyer purchases the business for $1.5 million plus 12% of gross revenue over the next five years. Owners should be careful with this option. It can be risky, since the owner will lose control of how the business runs after the sale, and there is no way to guarantee it will meet the owner's expectations.

Option Two - Sell a Minority Interest to Fuel Growth

A business can become more attractive to certain types of buyers as it increases in size. Business owners often have the potential to grow their business, but they need the capital to fuel that growth. With additional capital, they can make investments in new staff, products, locations and infrastructure to handle the increase in complexity of a growing business. When thinking of retirement, business owners may be less willing to risk greater personal investment in their business. They may also desire to start taking some of their hard earned equity out of the business. To do this, the business owner can sell a minority share of the business to an outside investor. Some of the proceeds go into the owner's pocket, and the rest will fund the growth of the business. While the owner is no longer the sole owner, the owner retains control in a minority interest recapitalization and can use an investor's funds to grow the business beyond what would have been possible without additional capital. When the business reaches the target size for the final sale, the business now commands a much higher sales price, which makes up for the fact that the proceeds will now need to be split with the minority investor. Think of it this way: The owner once had 100% of a small pie. After selling 30% of the company to fund growth and expansion, at the second sale they are now selling their 70% of a much larger pie. If all goes according to plan, 70% sale of a large pie could put more money in the owner's pocket than selling 100% of a smaller pie.

Option Three – Sell a Majority Interest:

This option is similar to selling a minority interest, except the business owner sells a majority share of the business and loses control of the operations. This can be a beneficial arrangement, if the owner is looking for an opportunity to decrease their role in the business but still stay involved. For example, an owner who really enjoys designing the products, but not running the day-to-day operations, can partner with an investor who will take over the operations and free the owner up to do more of the product design work. This enables the owner to take some of the equity of the business, diversify it into other investments and improve their personal financial position. Then, working with the new investor, the business can continue to grow. At the next sale, the minority interest will be worth more than it would have been before selling to the new majority investor.

Value Accelerate Before You Sell

In any of the options listed, a business owner should consider a Value Acceleration Plan first. Working with a Certified Exit Planning Advisor (CEPA) to create a Value Acceleration plan allows owners to increase the value of the business at its current size before bringing in an investor to fuel growth. A Value Acceleration Plan helps businesses mitigate risks and build procedures that will enhance the foundation of the company, so it is more likely to be able sustain growth. This ensures an owner will receive the highest price for the equity they sell after bringing in an investor. It also increases the likelihood that the growth plans made with the investor will be successful. And it means at each stage the business will be commanding the highest price, resulting in more value for the owner.

Owner Beware:

Selling a slice of your pie now so that you can take a few dollars off the table today and fuel growth may sound attractive. However, there are risks to consider. Pursuit of growth and expansion brings additional risk. This is unavoidable. No matter how well planned, and how well funded growth plans are, they come with no guarantee of success.

Additionally, owners no longer maintain complete control. Even if they retain a majority ownership of the business, no one is going to make a significant investment in the business without strings attached. An owner should make sure they do their own due diligence on the investor to ensure they are a good fit and are likeminded about what to expect after the transaction.

With these options, changes in how the business runs are inevitable. However, if the owner and new investor(s) have confidence in the growth plans and work well together, these options can help you get more value from your business than you ever dreamed possible on your own.

Contact Us:

Rich Gunn and Jasmine Menard-Lenczewski are the leaders of BPM's Value Acceleration Service Team, which helps with succession, transition and exit planning for business owners. Rich and Jasmine are both Certified Exit Planning Advisors and members of the Exit Planning Institute.

The Business Owners' Special Series (BOSS):

The Business Owners' Special Series (B.O.S.S.) is made up of several informational articles for business owners who are proactively seeking guidance from experts on how to implement value acceleration in their business. Be sure to keep reading, if you desire to develop your business to its maximum potential value and gain an understanding of how and why beginning the process sooner results in building greater value.