

# The Importance of Knowing What Your Business is Worth

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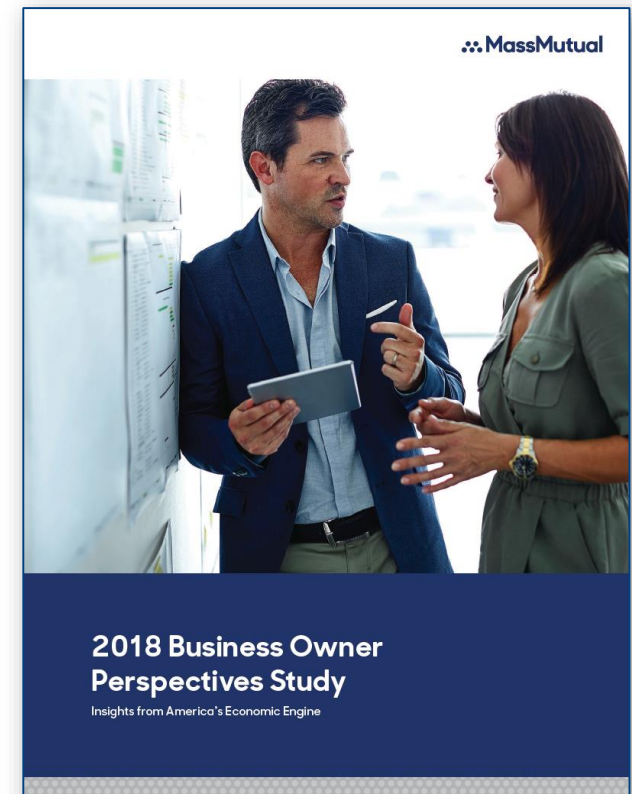
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# Methodology

Conducted by HawkPartners for Massachusetts Mutual Life Insurance Company (MassMutual), the study reveals that today's business owners are thinking about key business planning issues.

## Over 900 business owners surveyed.

- All with less than 500 employees.
- Nearly all in business 4+ years (91%).
- Over three-quarters with multiple owners (78%).
- Nearly all with family members in the business (91%).
- Most with annual revenues in excess of \$500K (74%)
- Most with household income in excess of \$100K (66%).



# Business Planning Core Pillars

Keeping key employees loyal

Knowing what the business is worth

Protecting the business from death of owner or key employee

Protecting the business from disability of owner or key employee

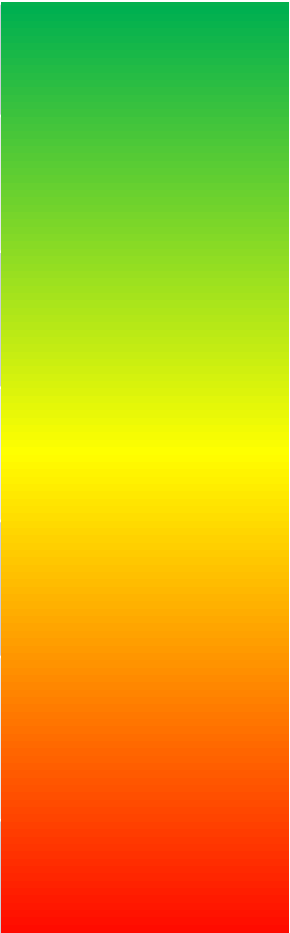
Business succession at death, disability or departure

Transitioning ownership and/or finding a buyer at retirement

Being fair and equitable on distribution of estate



# Core pillars at-a-glance

Core Pillar	Importance	2015 rank	How top-of-mind	Capability to solve	Who do they turn to for help?
Keeping key employees loyal		1	79%	56%	<ol style="list-style-type: none"> <li>1. My business partner and I would figure it out</li> <li>2. Financial professional</li> <li>3. Lawyer</li> <li>4. Family member</li> <li>5. Accountant</li> </ol>
Knowing what the business is worth		4	70%	52%	
Being fair and equitable with distribution of estate		7*	60%	51%	
Protecting the business from <u>death</u> of owner or key employee		3	53%	38%	
Business succession upon death, disability or departure		6	54%	43%	
Protecting the business from <u>disability</u> of owner or key employee		2	51%	41%	
Transitioning ownership/ finding a buyer at retirement		5	51%	43%	

# Business planning agreements in place

Will.....	74%
Estate plan.....	60%
Written succession plan.....	57%
Formal business valuation.....	51%
Buy-sell agreement covering death.....	46%
Buy-sell agreement covering disability.....	40%



# Common excuses

Why do business owners  
not have these plans  
in place?

"I don't feel like I need to think about  
these issues yet."

"I am too busy with the day-to-day  
management of the business, I don't have  
time."

"I don't have extra money to put towards  
addressing these issues."

"I would not know where to go for help."

"It is an uncomfortable conversation with  
my family/business partner."

# Common motivators

Why do business owners  
have these plans  
in place?

"I want to protect my family."

"I want to protect my business."

"I was doing personal planning and it prompted me to think about business planning."

"I want to protect my employees."

"A trusted source brought it up to me."



# The great unknown...will my business sell?

Nearly 60% of business owners say they plan to sell their businesses<sup>1</sup>...

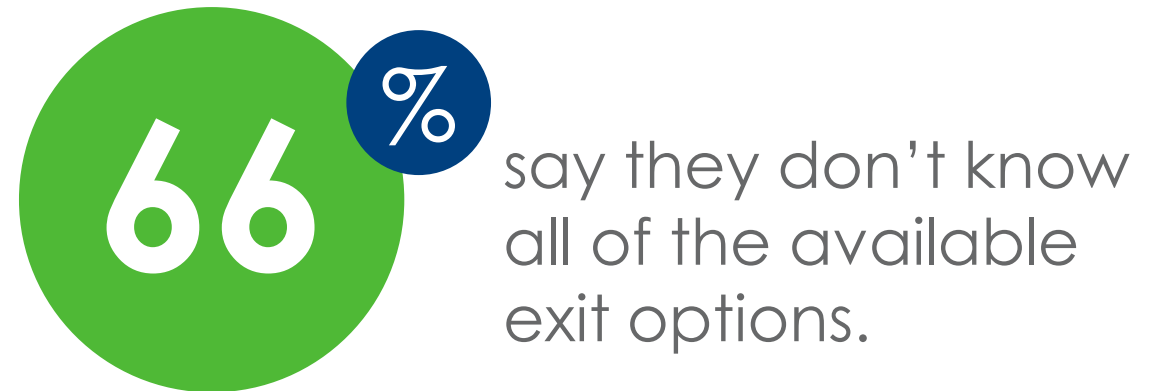
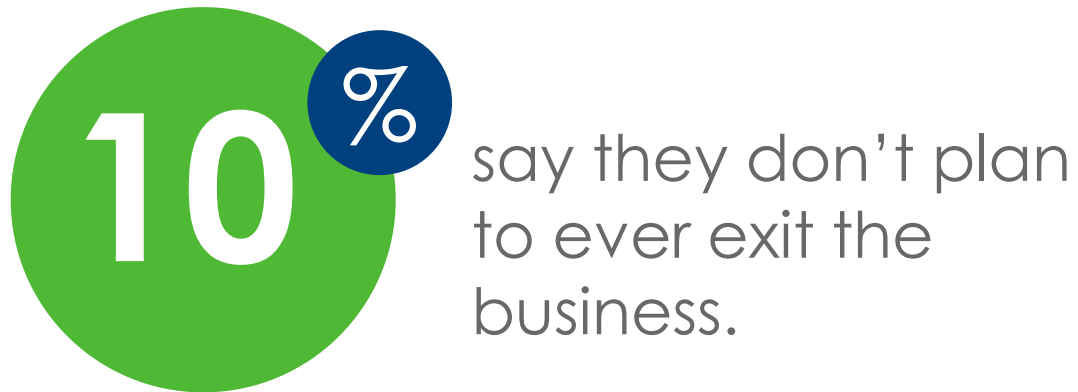


<sup>1</sup> MassMutual Business Owner Perspectives Study, 2018

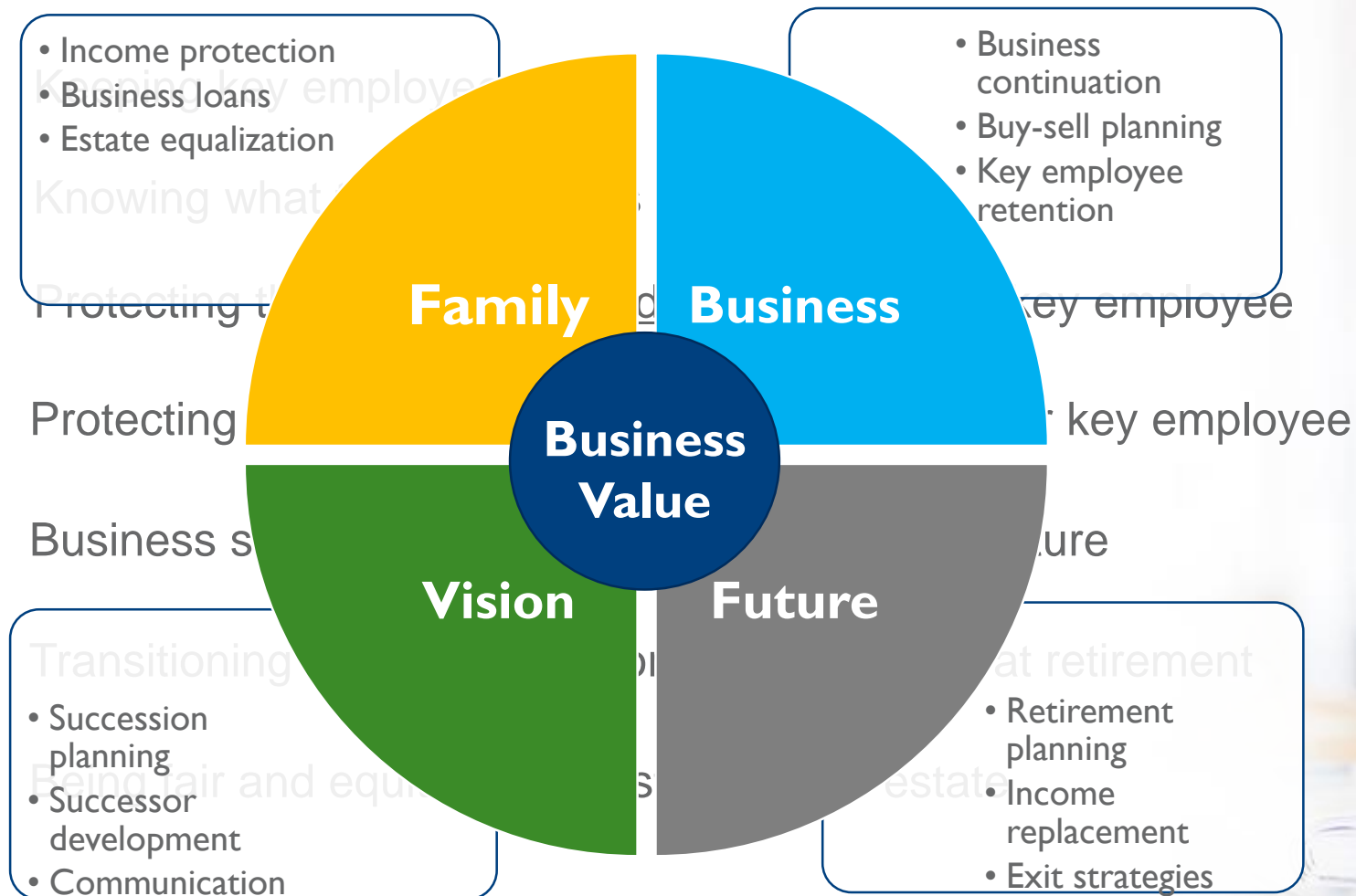
<sup>2</sup> Exit Planning Institute, State of Owner Readiness Survey, 2018

# The great known...will I exit my business?

**THE ONE STAT WE DIDN'T NEED RESEARCH TO PROVE:  
100% OF BUSINESS OWNERS WILL EXIT THEIR BUSINESSES!**



# Business planning core pillars, redux



# Knowing the true business value

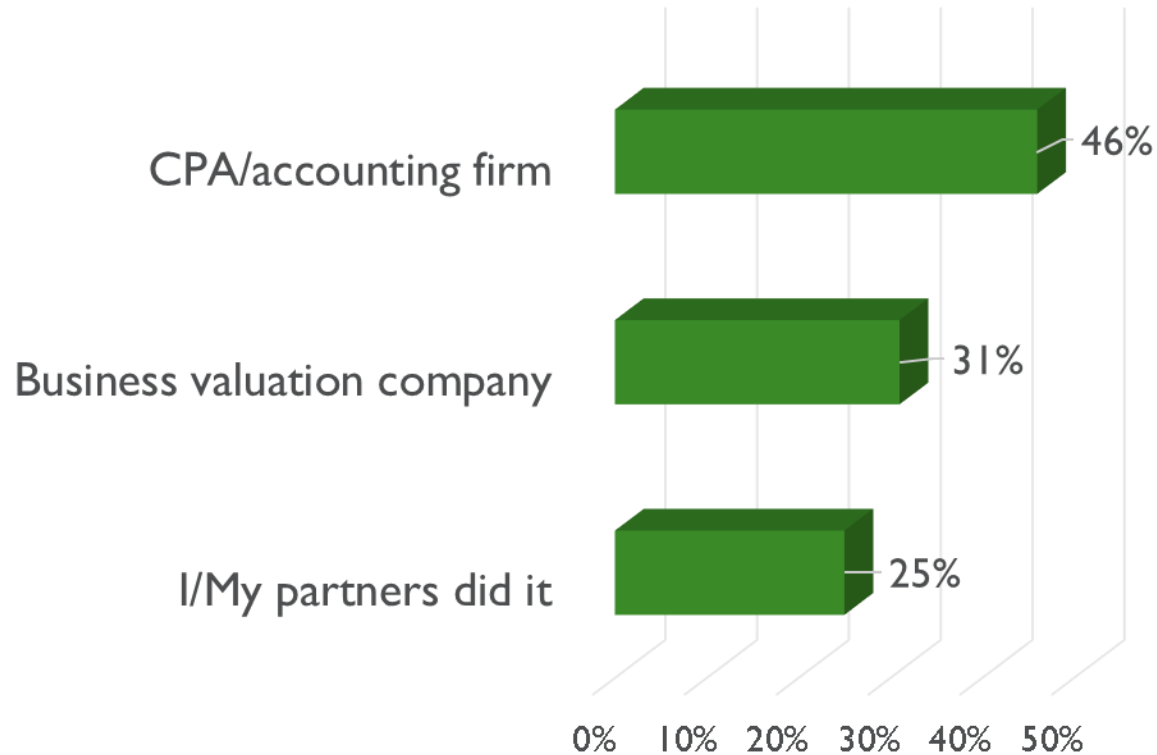


About half of business owners (59%) say they've had their business valued,  
but **1 in 4 valued it themselves!**



# Knowing the true business value

Who did the business valuation?





# Knowing the true business value

When business owners value themselves, the standard deviation can be 60%!



## The Four Capitals:

- Human capital
- Customer capital
- Structural capital
- Social capital

**Up to 80% of a business's value can be tied to intangible assets.\*\***

\*MassMutual Business Owner Perspectives Study, 2018

\*\*Exit Planning Institute, State of Owner Readiness Survey, 2018

# Business valuation wants & needs

**WANTS**

**&**

**NEEDS**

These are the  
“valuation milestones”

## I in 4 want a valuation to:

- Have another measure of business health/success
- Know if the business has value in the marketplace
- Prepare the business for sale

## Most need a valuation to:

- Fund retirement ahead (13%)
- Properly fund buy-sell agreements (10%)
- Fund any potential estate tax burden (10%)
- Equalize the estate for the heirs (9%)




# Stages of Value Maturity

1. Identify all assets and their value.
2. Protect the value by mitigating personal, financial and business risks.
3. Build the value by prioritizing strategic actions that impact cash flow and improvements to the multiple.
4. Harvest the value by exploring ways to extract the wealth trapped in the business.



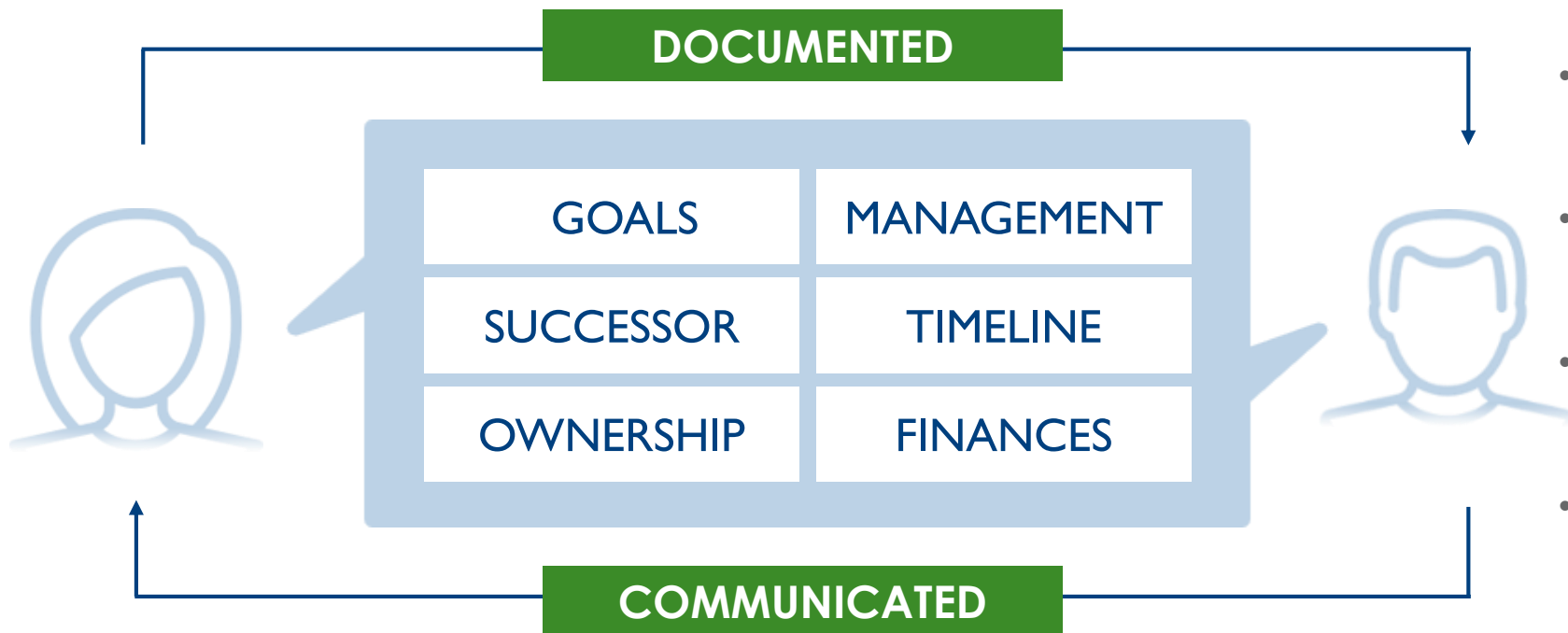


# Business value and succession planning

A man in a light blue polo shirt with a logo on the chest is looking down at a laptop. He is outdoors, sitting on a bench near a large fountain with water spraying upwards. In the background, there is a brick building and some trees.

Less than half of business owners have a **buy-sell agreement** in place, and of those who do, *over half may not be properly funded.*

# What goes into a good succession plan?



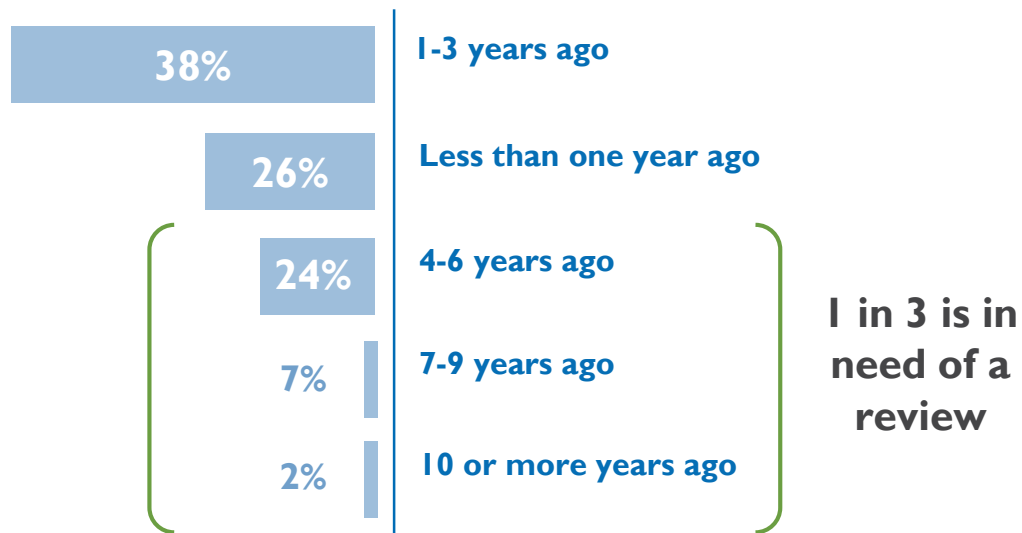
- Goals: What do you want out of the business when you exit?
- Successor(s): Who will take over and are they prepared?
- Ownership: What will future roles and percentages look like?
- Management: How will you keep them onboard through the transition and beyond?
- Timeline: Have you documented the steps with specific milestones?
- Finances: Where will the funds come from for a buyout; will there be tax implications?



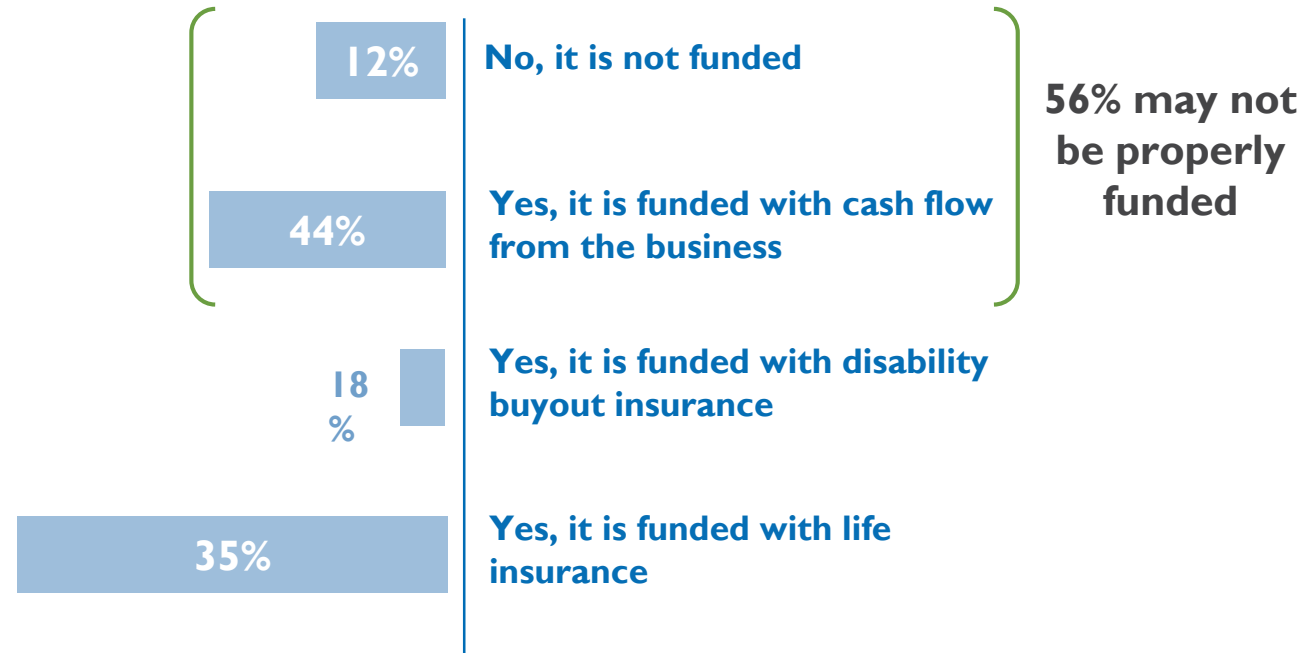
# Business value and succession planning

Business owners have stale agreements in place, leading to underfunded agreements.

## When was the last time your buy-sell agreement was reviewed?



## Is your buy-sell funded?



# Red flags of buy-sell agreements

- Established incorrectly based on business entity type.
- Established incorrectly based on number of business owners.
- Doesn't account for all five D's (death, disability, divorce, departure, disqualification).
- Inconsistent definition of what is considered "disabled."
- No proper valuation has been placed on the business.
- The agreement isn't funded.
- The agreement isn't signed.



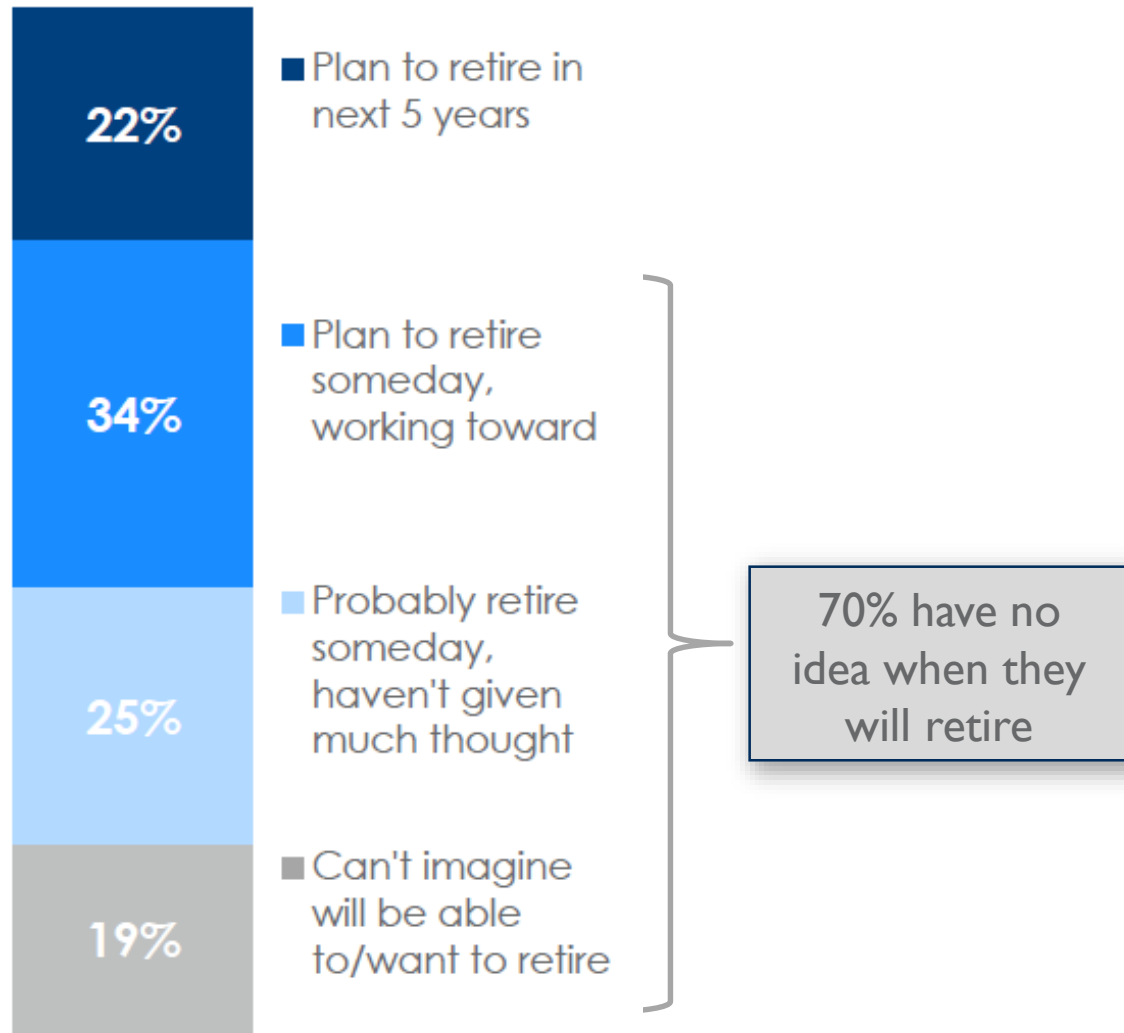


# Business value and retirement planning

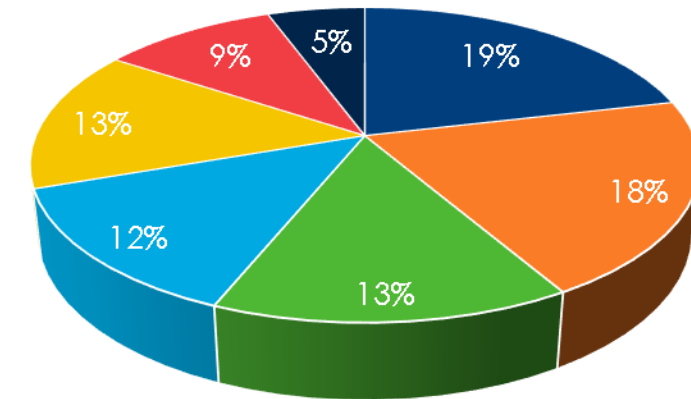


Most business owners have no idea when they plan to retire, and 1 in 3 don't have any retirement assets outside their business.

# Business value and retirement planning



## How will retirement be funded?



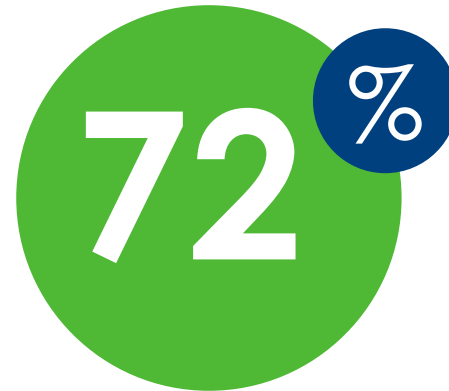
- Personal savings
- Retirement accounts
- Social security
- Sale of the business
- Income from business
- Real estate
- Pension plan

3 out of 4 have less than \$500k in their retirement accounts and household investable assets

# What is the most important “valuation method”?

## Approaches to valuing a business:

- Book value
- Market value
- Capitalization of earnings
- Discounted cash flow
- Asset accumulation
- Liquidation value
- **Income replacement value**



don't know or don't think their exit will impact their lifestyles\*



# What is the most important “valuation method”?

*the Rolling Stones* said...

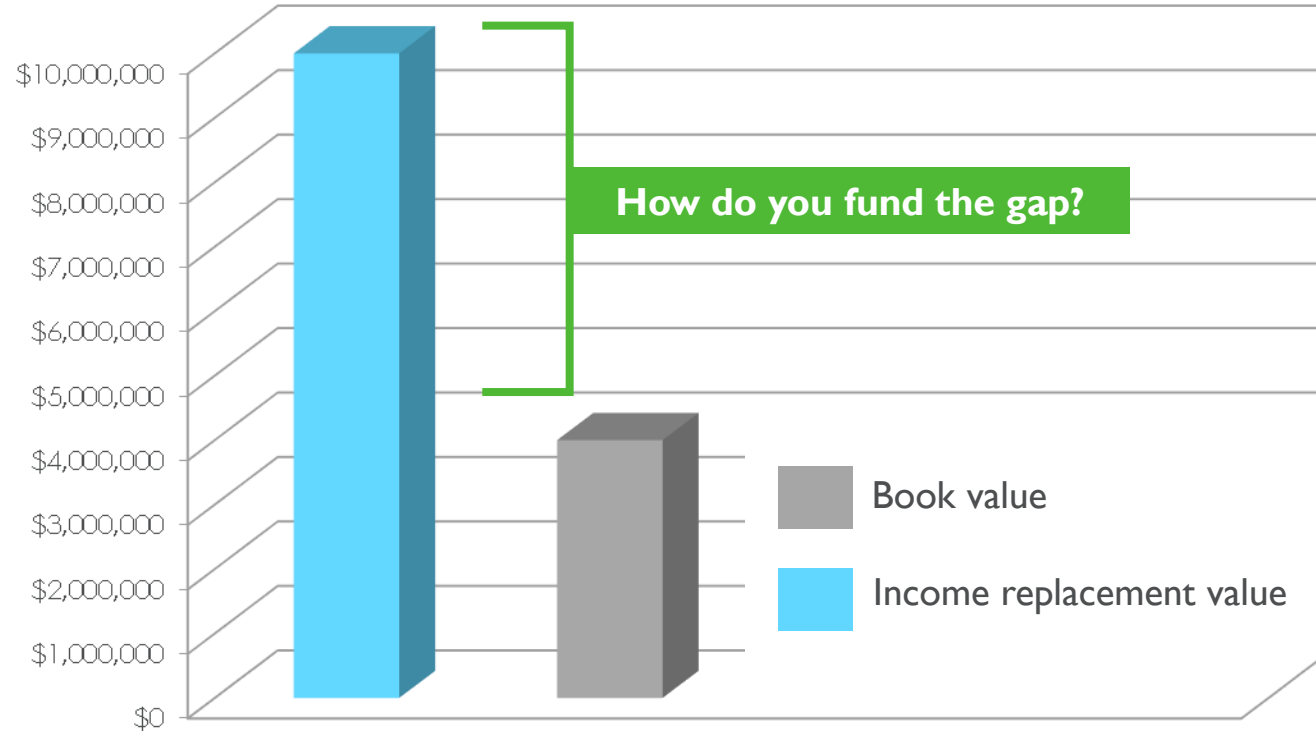
**You can't always get what you want,  
but if you try sometimes you get  
what you need.**

What is the personal value you receive in the form of compensation and other benefits?

- Salary
- Pension, profit sharing, etc.
- Employee benefit programs (insurance)
- Company paid car, travel, meals, etc.
- Rent paid to owner's real estate entity
- Other company paid benefits not listed above (stock options, etc.)

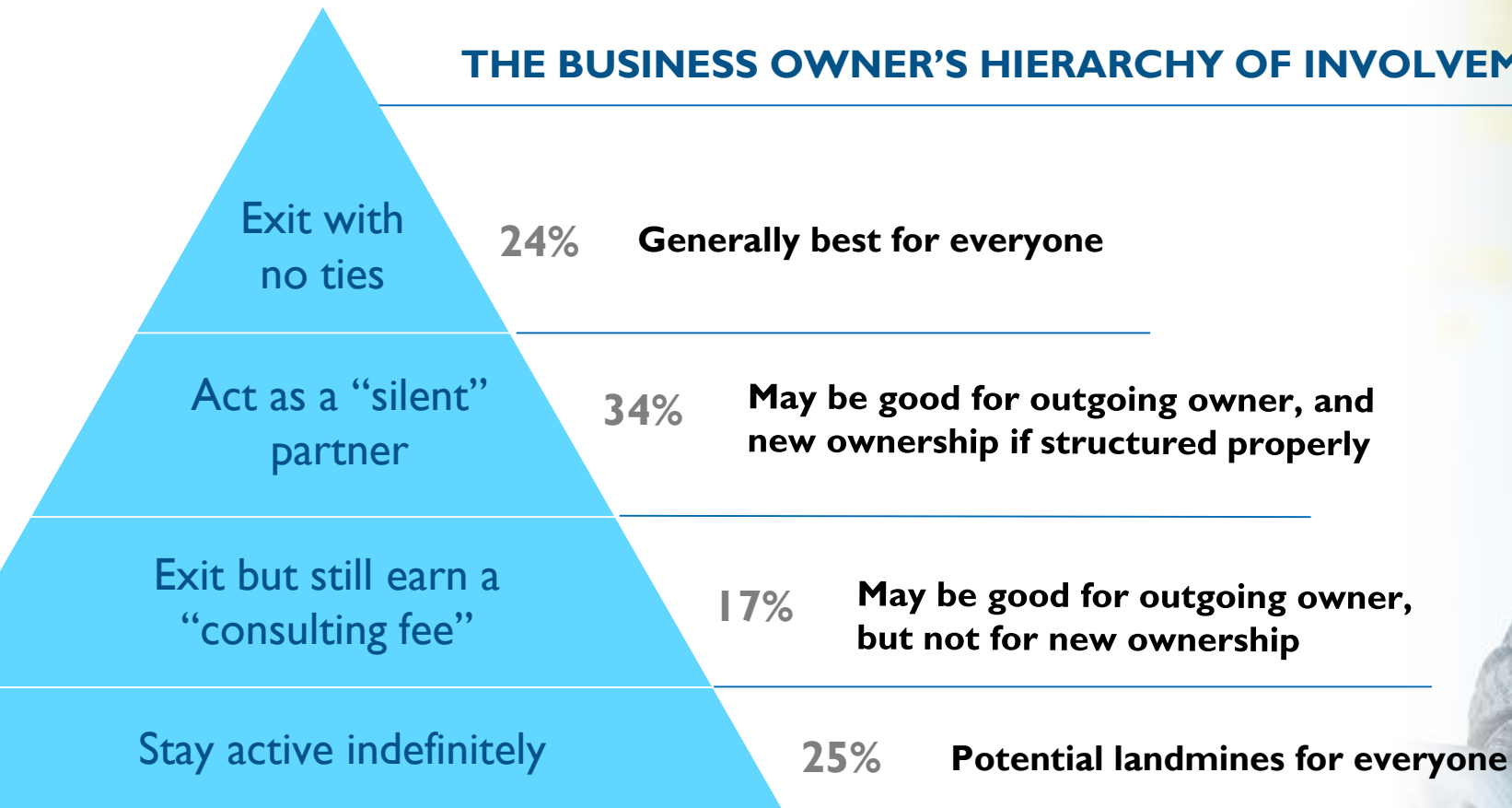
# Determine the income replacement value

**Income replacement** value is about what you need the business to be worth vs. what you think it is worth.



# Business value and retirement planning

## THE BUSINESS OWNER'S HIERARCHY OF INVOLVEMENT





# Business value and estate planning



Two-thirds of business owners say the business is their **largest asset**, and over half plan to divide it equally among all children.

# Estate planning for business owners

As a business owner, there are special estate planning considerations:

**ESTATE REDUCTION:** ► Gifting of business ownership while you are alive.

**ESTATE LIQUIDITY:** ► Avoiding forced liquidation of business assets to raise cash.

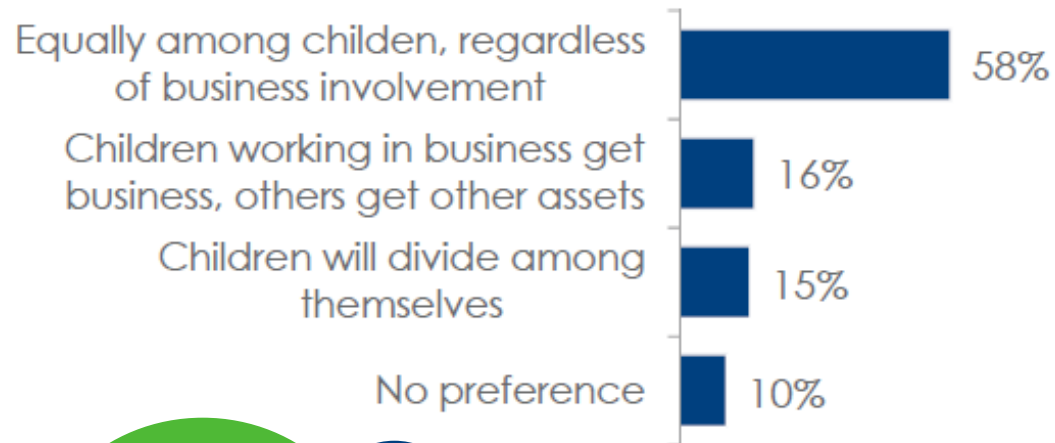
**ESTATE EQUALIZATION:** ► Being fair when not all family members are working in the business.

**BUSINESS VALUATION:** ► How, and by whom, will the business be valued at your death?



# Business value and estate planning

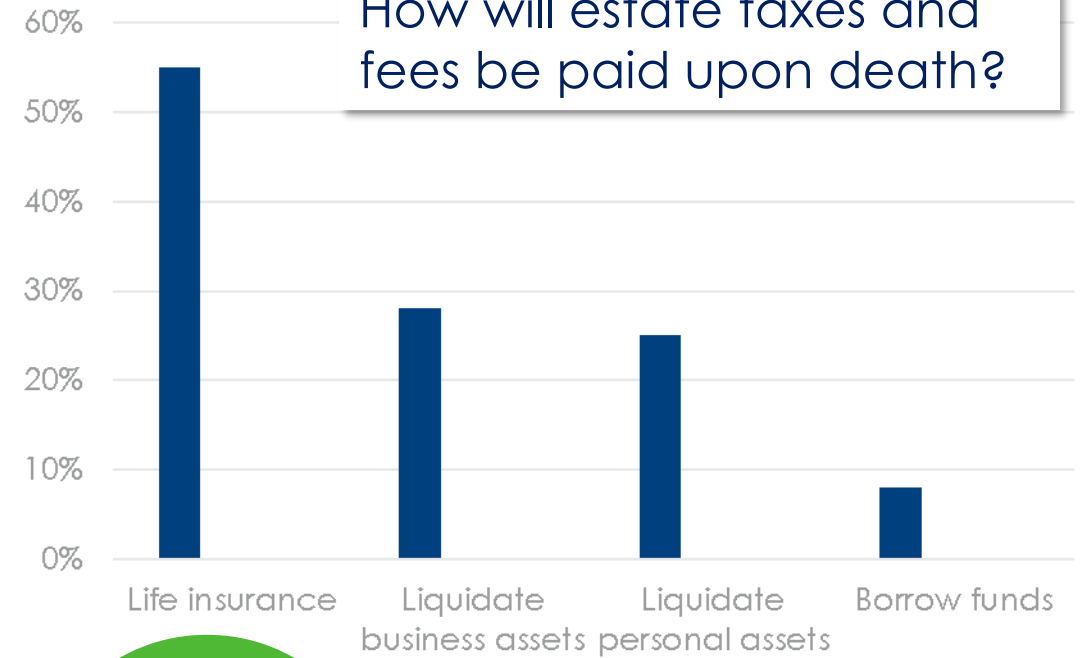
How will you divide the business assets in the estate?



**84%**

Have no plan for estate equalization

How will estate taxes and fees be paid upon death?



**1 in 4**

May have to liquidate assets to pay estate taxes

# Estate equalization

**DISTRIBUTING OWNERSHIP IN  
THE BUSINESS TO THE NEXT  
GENERATION FAIRLY.**



**WHEN IT COMES TO THE  
BUSINESS, FAIR DOES NOT  
ALWAYS MEAN EQUAL.**

**Estate equalization involves making some hard decisions:**

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- Should the business be divided equally between children working in the business and those not involved in the business?
- If the children not involved in the business don't receive ownership, what other assets can they receive that are equal in value?
- Are you comfortable with children outside the business receiving liquid assets versus those working in the business receiving an illiquid asset?
- Those working in the business may begin receiving their inheritance today in the form of ownership, whereas those not involved must wait until death to receive theirs.

# The paradigm shifts

## OLD

### **Know the value.**

- It's not solely a mathematical equation

### **Be a lifestyle business owner.**

- Don't focus on income

### **Focus on the “emotional” or “intrinsic” values.**

- It's not about what you perceive it be worth or what its worth to me

## NEW

### **Understand the value.**

- Understand the value drivers

### **Be a value accelerator.**

- Focus on enterprise value

### **Focus on the intangible assets.**

- These drivers a business's attractiveness

