

July 2020

The Arithmetic of Ownership Transition Planning

By Franco Silva

For many business owners of privately-held companies, the transition of their ownership is an uncharted path. It is important to realize upfront that time is a precious commodity when planning such an event. The more time you have, the higher the probability that you will be able to ensure a successful ownership transition event.

Additionally, one of the most important components of the planning process is an assessment of your company's internal infrastructure and management team and any additions or adjustments that must be made. The strength of your infrastructure and management team, or lack thereof, can greatly affect the value of your business and the outcome of your ownership transition. Having a strong internal infrastructure and management team in place can facilitate a more successful and more profitable ownership transition. On the other hand, if your business lacks a strong internal infrastructure and management team, you may suffer a less-than-desirable outcome during the ownership transition process.

For a closely-held business that lacks internal management beyond the business owner, the establishment of a strong management team is critical. The reality for many owners of closely-held businesses is that they are not only the owner but also chief buyer, chief financial officer, salesperson and janitor. If the owner wears every hat, the business is weaker when that owner leaves, so it is vital to the value of the business to have a strong, independent management team in place before the owner exits.

The arithmetic of ownership transition should encompass the following key steps.

1. Proactive Planning

As the owner of a closely-held business, it is critically important to plan early for your ownership transition event. If you plan early enough, you will have more exit options available and be able to create a time frame that is best suited for all stakeholders. The reality is that some elements of preparation can be accomplished quickly, while other elements may require several years.

As you begin the planning process, you should ask yourself the following questions:

1. Where do you see the ownership of your company in the next five to 10 years? What do you want your legacy to be?
2. Where do other owners of your company see its ownership in the next five to 10 years? What do they want the legacy to be?
3. Are the timelines the same? Are the values the same?
4. What exit strategies are available that will meet these expectations?

These questions help define the blueprint and time frame of an ownership transition event.

2. Build Your Management Team

The second step is to secure your management team and improve your internal infrastructure. To build your management team, identify the most appropriate executives for your business and clearly define their roles and responsibilities. Implement mentoring and formal training for your organization's next generation of leaders to gain the bench-strength you need to best transition your business into the future. Then look for ways to improve organizational processes and procedures. Hiring the right people and building a strong infrastructure will help your business achieve the highest value when it is time to transition ownership.

3. Achieve Your Ownership Transition Goals

The third step is taking your business to market, whether for an internal or external ownership transition. Your business will be much more attractive to prospective buyers if it has a strong internal management team in place with a well-developed internal infrastructure. Also, lenders will be much more likely to lend money to an established, productive management team. Once it is ready to be sold, the valuation of your business will reflect the internal investments you have made since value is most often based on ownership structure, management size, growth potential and visibility, among other marketplace factors.

At Prairie, we work with business owners to determine where they fit within the valuation tier. We then help find the most appropriate buyer at the most favorable price and terms in the marketplace. When business owners make these critical investments in infrastructure and internal management, they reap the rewards, and that arithmetic adds up to more dollars and cents for them at ownership transition time.

For more information, contact:

Franco Silva, Director

Prairie Capital Advisors

fsilva@prairiecap.com

312.445.9213