HOW TO SELL YOUR TAX OR ACCOUNTING PRACTICE

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INTRODUCTON

Seeking the Best Deal for You and Your Clients

Every practice at some time will be either: 1) Sold to a third party; 2) Sold or passed onto an heir, partner or employee or; 3) Be abandoned. If you decide to sell your practice, you will want to find the best Buyer and structure the best deal that will assure that your clients are taken care of and that you maximize the overall return from your years of hard work. Since it is customary in accounting practice sales for the Seller to guarantee the gross revenue for one year, and for the Buyer to be an educated and business-wise accountant, you will want to prepare your practice and sales package expertly, completely, and with an eye toward maximum transfer of goodwill. The Buyer's success will directly affect your overall return of investment. This report addresses the steps necessary to maximize your overall return.

I. TIPS FOR SELLING YOUR PRACTICE

A. A FAVORABLE PRESENTATION

If you want top dollar for your practice, you should make sure that your practice is running smoothly and efficiently and it looks good to a potential Buyer. The Buyer can make his decision based only on what he sees. Take all efforts to have a good staff, good organization, up to date equipment (all serviced), and up to date client files. Most owners are remiss in handling these matters in their own business. This is one time when the extra effort will really pay off, not only in the original sales price, but also over the long haul in the Buyer's success (and ultimately debt service).

B. RAISE FEES TO MARKET LEVEL

Some practitioners purposely do not raise fees prior to a sale because they feel that they may lose some clients thereby reducing the gross revenue and hence, the sales price. On the contrary, most Buyers would rather purchase a practice that has had regular fee increases on a yearly basis including the year before the purchase. Such a policy ensures a continuing growth pattern, less chance of client fallout and a higher price upon sale. Obviously, this also produces higher cash flow for you (while you are in the practice) and for the Buyer to repay the debt. When the Buyer does take over, he should continue your policy of fee increases unless the fees are substantially below market.

CASE HISTORY: One practice we sold had 800 individual tax returns with very low fees. The Buyer raised fees about 20% each year for 5 years. Each year he lost about 20% of the clients but more than made up the difference with increased fees and an overall increase in gross revenue. The result was the building of a $37,000 practice into over $100,000 in that period of time.

C. ACCOUNTS RECEIVABLE

Excessive accounts receivable can cause a severe cash shortage for the Buyer during the most critical time. Since the accounts receivable are usually handled on a first-out basis, the Seller gets paid first, leaving a real drain on the Buyer. A typical accounts receivable amount would be 30 to 60 days. Accounts receivable greater than this can be handled either by: 1) Adding them to the sales price; 2) Offering a moratorium on payments for 2 or 3 months; or 3) The Seller carrying back a note for 6 to 12 months. Of course, the best policy is for the Seller to tighten up his credit policy and keep the receivables well in line. It would be very difficult for the Buyer to change the clients paying habits. If the new Buyer attempts to collect faster, there will most likely be bad will created resulting in a fallout of clients, harming both the Buyer and Seller.

D. OFFICE ORGANIZATION

When the Buyer takes over the practice, he will be extremely busy meeting your clients, reviewing workpapers, and learning your office procedures. A well-organized office will ensure his success in your practice. Particular attention should be paid to having adequate client data (e.g., engagement letters, client fact sheets, etc) and easy to follow workpapers. Remember, you may have much of this information in your head, but the Buyer will be lost without it.

An adequate staff is often essential to a successful transition. After your short introductory period, the Buyer has to be able to rely on your personnel for both work output and personal characteristics of your clients. It is a good idea to have your staff at market wages or salaries, eager to help the new Buyer become a success. Disgruntled or underpaid employees could undermine the success of you and the Buyer or possibly attempt to steal some of the clients away.

CASE HISTORY: One practice we sold in South Bay was very well organized and had a complete staff, which resulted in a 37% increase in business the first year of possession by the new Buyers.

E. SERVICES MIX

Approximately 85% of the Buyers in our database would prefer a practice with a services mix of about 60% accounting, 30% tax, and 10% MAS, and about 15% of the Buyers would prefer only tax preparation services. This is because most Buyers need the monthly cash flow for debt service and for family commitments. There are only a few

Buyers that want any audits due to liability and distaste from prior CPA training programs. Over the last several years, many accountants have sought to increase cash flow by offering additional services such as financial planning. In short, a practice with a steady cash flow and an eye to the future is most desirable.

CASE HISTORY: A Seller we represented in San Fernando Valley with billings derived 80% from accounting and priced at l.19X gross produced 124 inquiries and 9 offers. The practice sold for the listed price.

F. SALES TERMS

You as the Seller probably want all cash and of course the Buyer wants to put nothing down and pay you back with a percentage of your profits. The reality of an accounting practice sale is that the marketplace has been active enough to produce an "efficient market" where a large number of Buyers and Sellers have established certain standards and rules of thumb. Some of these standards are: price and down payment, extent of covenant not to compete and value thereof, allocation of sales price for tax purposes, payback period and interest rate, reasonable guarantee of the gross revenue, and structure of sale. (For example, a sale with a contractual amount in terms of a promissory note or a sale based on a percentage of billings over several years. We favor the promissory note since this allows for recovery in case of default or breach of contract).

G. SET A REALISTIC PRICE

A "realistic" market price can only be one that allows a reasonable return on the Buyer's investment. The fair market price includes consideration of the past and future earnings of the company. Too often the Seller sets an unreasonable price, one that is too high and produces a low return on investment. This is usually because the owner has spent his lifetime nurturing a practice which is as much a part of him as a son or daughter.

The Seller usually places a "psychological" value on the practice far above the "market" value. Because of the wide difference between the “value” of the practice placed by the Seller and the fair market price, the Seller oftentimes is in for a tremendous letdown or he spends years trying to sell his practice.

CASE HISTORY: A practitioner in the Inland Empire foothills wanted to sell his practice for 100% of one year's gross even though he devoted 85% of his time to his professorship at a nearby prestigious university. After several months of trying to sell the practice himself he hired us to handle his sale. His key employee had just left and opened up an office within a few blocks. We sold his practice, but had to provide a longer than usual fallout provision to protect the Buyer. If the Seller had taken certain steps a few years prior to the sale, he could have "normalized" his practice and realized a much better deal.

H. ESTABLISH A VALUE FOR THE BUSINESS USING STANDARD APPRAISAL TECHNIQUES RATHER THAN USING RULE OF THUMB RATIOS

Sellers often use rules of thumb in determining the value of their Businesses. These are frequently quoted industry standards or "multiples" that oversimplify the answer. While often a rule of thumb can give one an approximate "rough" value of a practice, a complete analysis should be performed to accurately establish the true value of a practice.

The overriding consideration for the price and terms of any practice is: "Will the practice being acquired pay for itself over a reasonable length of time?" A knowledgeable Seller will provide a projected cash flow-debt retirement schedule to the Buyer to prove that his practice will provide a reasonable return on investment.

HINT: By offering flexible terms in the full price, payback terms, interest rate, and down payment, the Seller may seek to maximize that objective which is most important to him.

I. ASK FOR A REASONABLE DOWN PAYMENT

Obviously, most Sellers would like to sell for as much down payment as possible. However, a high down payment often puts the practice out of range for most Buyers. Those Buyers that do have the money want to leverage the sale.

Another consideration, with respect to the size of the down payment, is how much working capital will be left for the Buyer as well as his plans for capital equipment expenditures. For example, if the Buyer has to put in new equipment to increase the profitability of the company, the Seller should not negotiate all of the Buyer's available funds nor a large down payment.

If the Buyer becomes financially "strapped" and has considerable difficulty turning a tired, old practice into an expanded, profitable one because of lack of working capital, both parties will eventually lose.

TAX CONSIDERATION: Another reason for a low down payment is for tax considerations. The Seller needs to analyze and balance the tax implications with the return on investment of the remaining proceeds from the sale after the tax is paid. In other words, if the Seller can receive 10% on the promissory note from the sale of his business, is this better than taking a larger down payment, paying taxes on it, and then investing the remaining proceeds at a current savings rate of maybe only 5%?

J. OFFER A REASONABLE PAYOUT PERIOD ON THE PURCHASE PRICE

Visualize yourself buying a competitor's company with the same price and terms that you are asking for your practice. Would you be able to make it a profitable investment out of its own cash flow and have enough cushion left over? Too many times the Seller feels the Buyer should use other income to support the investment. An intelligent Buyer demands that an acquisition stand on its own financially.

K. PROVIDE GOOD FINANCIAL AND SALES RECORDS

Too often the Seller gives the Buyer poor records with which the Buyer is to make a business decision. Sometimes the Seller refuses or resists in making available the type of data an informed Buyer wants to properly evaluate a practice. Other times the

Seller will state, "the profit and loss statement looks poor because of the amount of money I take out of the practice in other ways". Don't expect the Buyer to knowledgeably act on such generalizations. He will be hearing these types of statements from many Sellers. Reconstruct your financial statement for the fringe benefits you and your family take out of the practice so that the true profits and cash flow can be reflected. One word of caution: present a financial statement to the Buyer that you can prove is fair and that you can warrant. If you do too much boasting about your practice and it can be proven these statements were misleading, you could be later sued for misrepresentation.

TIP: We have frequently taken practices with skimpy records and, by preparing a complete client ledger, have been able to sell the practice at the market price.

L. VIEW THE SALE FROM THE BUYER'S POINT OF VIEW

Undoubtedly the most successful transactions we have participated in were those where the Seller and the Buyer put themselves in the other man's shoes and worked out a plan for items such as the down payment, terms, working capital, tax considerations, the allocation of the purchase price, etc.

The Seller should realize that in selling a practice the return on investment has to be greater than a more secure investment (i.e. bonds, savings accounts). The return on investment (ROI) on a practice has to be in the range of 20% to 33%. For example, a $200,000 a year practice produces a 25% profit (before taxes and after owner's draw) equal to $50,000. For a Buyer desiring a 25% return on his investment, the purchase price would be $200,000 (for the goodwill, only). A 20% ROI would yield a purchase price of $250,000. Unless there are extraordinary factors, do not expect the purchase price to be much higher than this.

Don't expect the Buyer to settle for a return on investment much less than 20%. He has to borrow money from the bank at anywhere from 11% to about 15% (depending on the borrowing rates at the time) to buy your practice and assume the inherent risk of a business while hocking the family fortune.

COMMENT: By applying the Excess Earnings method of appraisal to tax, bookkeeping and accounting practices, you will find that after adjusting for thc capitalization rate, earnings for a replacement manager and excess earnings, most practices will be worth a value approximately equal to 100% to 120% of their gross revenues. Hence, the frequent use of the "rule of thumb" in accounting practice sales.

M. ACKNOWLEDGE THE IMPROVEMENTS THE BUYER MUST MAKE IN THE BUSINESS

Many businesses are sold because of the age or lack of working capital on the part of the Seller. The Seller should forecast the type of capital improvements the Buyer must make to continue. We have seen many cases where the Seller has not put any major improvements into his or her practice for the last 10 or 15 years and has been living off his or her depreciation.

Because of this the Buyer might be acquiring a physically depleted practice which requires significant investment to overhaul the equipment, buy new machinery, or obtain the labor-saving devices or personnel necessary to operate at a reasonable profit. For this reason some Sellers wisely allow the Buyer some breathing room by deferring principal payments for a period of time to allow for a reasonable cash flow to sustain and improve the practice. Of course, a good down payment is made for security.

N. LEAVE THE QUICK ASSETS IN THE BUSINESS

Too often the Seller wants to take all of the cash, accounts receivable, and even pieces of equipment out of the business. Stripping the practice of such assets means the Buyer has to replenish these and if this is not clearly understood at the time of the purchase, it could mean the Buyer would have a difficult time. If the practice is large, say over $400,000 gross, then by stripping the practice of its working capital (i.e. cash, accounts receivable, etc.), a tragedy could occur with the Buyer not being able to make the payments and thereby defaulting, to the loss of both the Seller and the Buyer.

O. USE YOUR PROFESSIONAL'S SERVICES PROPERLY

Your lawyer and other professionals should be used in their areas of expertise; however, they cannot make the final business decision, which is yours. Your lawyer can advise you on legal matters and your banker can advise you on matters off financing. It is just as wrong to overuse their advice as it is to discount them completely.

COMMENT: Business Brokerage prepares a complete Buy/Sell Agreement since most lawyers are not familiar with an accounting practice sale. We welcome the Buyer and Seller to provide this agreement to their lawyers for review.

P. EXPECT TO SELL TO AN INDIVIDUAL OR A BUSINESS ABOUT THE SAME SIZE AS YOURS

Ernst & Young, Peat Marwick, and other firms like them rarely buy a company doing under a million dollars in sales. They have to apply their costs and expenses to your gross fees and simply cannot make a profit on a practice without their fee structure. If you do sell to a large practice, remember, they will only be human in wanting to "cherry pick" the big clients and neglect the smaller clients. Be realistic about to whom you want to sell. Look to the individual practitioner or small firm if you are selling a practice under a million in gross.

COMMENT: We can usually find a Buyer for a large practice who can obtain adequate funds by leveraging his real estate. (Note: this has varied over the years depending on the real estate market and natural disasters such as the Northridge earthquake).

Q. SELL YOUR BUSINESS WHEN BUSINESS IS GOOD

One of the most serious errors a company can make is to put off selling. The best time to get a good price for your company is when business is good.

R. DON'T JUMP AT THE HIGHEST PRICE OFFERED

If you're getting a sensational price, make sure that's all you're getting. Investigate the Buyer thoroughly.

COMMENT: We provide the Seller with a TRW credit check of the Buyer prior to finalizing the deal. This has paid off more than once.

S. LOOK OUT FOR THE FLASHY CHROME

Sometimes a Buyer in his big car and fancy home office building may not be as secure as he appears. Some Buyers with plush corporate offices are out buying companies (for paper) when they can hardly make ends meet in their own companies. Look beyond the chrome to see if there is ability and security behind the Buyer.

T. EXPECT THE BUSINESS TO BE THE SECURITY

For most transactions, the Seller gets back as security the business he has sold. Very seldom does a Seller get more than a dollar of collateral for a dollar of practice sold.

COMMENT: When we list a practice for sale, we provide three (or more, if desired) pricing scenarios for the Seller. This way he can balance the various factors of his price, down payment, terms, and security to meet his need.

U. EVALUATE YOUR INVESTMENT IN THE BUYER

As most companies are sold for a combination of cash and notes, the Seller is in effect making an investment in the Buyer. Look into the managerial and personality characteristics of the Buyer as well as the financial.

HINT: The most successful accountants that we have seen possess strong communication and "people" skills.

V. CONSIDER THE ADVANTAGES OF USING BUSINESS BROKERAGE

Know how to use a broker. A reputable broker, such as Business Brokerage, can help you determine a fair price, terms, methods of payment, and allocation of assets. He will also incorporate the psychological requirements of the Buyer and Seller into the transaction.

A good broker will in effect help both the Buyer and the Seller although he nearly always receives his fee from the Seller. The reason he helps both the Buyer and the Seller is that he wants to see the fairest possible transaction to both sides and one that will be satisfactorily effected over the terms of the payments.

With a good broker, you can take advantage of "third party" negotiations. Let him get completely involved in all correspondence and meetings between you and the prospect. Many a transaction has been lost because the Seller wanted to handle the process all by himself. The "courtship" and negotiating process is delicate. A competent broker can be an effective middleman.

A reputable practice broker will give you his references. Because he works on a commission basis, he tends to be eager to complete the transaction. This "eagerness" can be a useful motivating factor to the transaction.

HINT: By using Business Brokerage, a broker that specializes in accounting & tax practice sales and that advertises aggressively, you will be sure that your practice is exposed" to a great many Buyers. With several Buyers interested and bidding on your practice, you will be sure to get the best deal.

W. DO NOT LET THE BUYER COME INTO THE PRACTICE ON A "NO DOWN" PAYMENT OR "TRIAL" PERIOD

Buyers often ask if they can come into the practice to work for a while and see if the practice "fits" them. With good intentions on the part of the Buyer, your damage might only be that the Buyer makes some errors and/or omissions, or that some of the clients like his personality better than yours and prefer to go with the Buyer if the Buyer doesn't complete the deal. With bad intentions on the part of the Buyer, your damage could be that he learns all of your systems (including any weakness that he could use against you), obtains your client list, and fee schedules, and goes down the street, opens an office and actively solicits your clients.

HINT: Our experience is that a strong Buyer who is confident of his abilities and experience, and forthright in his intentions, is quite willing to perform his due diligence, enter into a buy/sell agreement, and proceed with the deal by putting up a substantial down payment.

X. THERE ARE "GUARANTEES" AND THERE ARE "GUARANTEES"

Since it is customary that in order to get the highest price in your sale you will have to guarantee the gross revenue for the first year of possession, be sure that the guarantee is fair to you as well as to the Buyer. For instance, there is a popular CPE seminar on buying an accounting practice that recommends that the Buyer offer to pay the Seller 20% of the receipts collected over a period of 5 or 6 years. To us this is unconscionable: that a Buyer would ask a Seller to turn over his business that has provided the Seller and his family a living for years to a Buyer with 1) no down payment, and 2) effectively, ask the Seller to guarantee the Buyer's success for 5 or 6 years. Shouldn't the Buyer take some of the risk!

COMMENT: If a Buyer offers you an earn out deal, be sure to consider all of the downside risk, because he will tell you only of all of the upside potential.

II. A PROFILE OF THE BUYER

The accountant is professionally trained and experienced in the analysis of businesses. He is also trained to look for discrepancies, errors, and omissions in financial data. In short, he is careful and not prone to take risks. He studies the data, and will not be coerced into purchasing your practice.

With this in mind it only follows that you should prepare a complete “prospectus" on your practice with all of the pertinent data included. Your package should be prepared with the utmost integrity and fully cover the following items which are key to establishing value:

A. RETURN ON INVESTMENT

1) Fee structure 2) Itemized expenses 3) Services mix 4) Billing policies, collections, A/R's 5) Cash receipts on a monthly basis 6) Hours of operation, billable hours 7) Profitability 8) Historical record.

B. QUALITY

1) Customer list: by industry, sales, type, fees, years serviced, services provided 2) Client files: quality of workpapers, product 3) Office organization 4) Location services performed 5) Manner of conducting practice. 6) Location: community demographics. 7) Research library used

C. CONTINUITY AND PREDICTABILITY

1) Covenant not to compete 2) Guarantee of gross revenue 3) Introduction to clients 4) Reputation in the community 5) Age of practice/age of accounts 6) Staff: function, years with firm, experience 7) Professionalism of Seller 8) Overall appearance of practice.

D. POTENTIAL SAVINGS AND TAX SHELTER

1) Lease: terms and conditions. 2) Synergistic possibilities 3) Computer services used 4) Furniture, fixtures and equipment 5) Terms and conditions of sale, financing 6) Allocation of consideration.

III. STEPS REQUIRED TO SELL YOUR PRACTICE

A. GATHER ALL OF THE PERTINENT DATA.

Bring all of your financial statements up to date and assemble the last three years statements along with your premises lease and any other equipment leases or contracts that you may have.

B. RESTRUCTURE THE INCOME STATEMENT

Most small businesses (especially sole proprietors) try to minimize net profit in order to minimize taxes. Of course this represents a problem when you want to sell your business in terms of selling price and structuring debt service. Therefore, you must restructure your income statement by making adjustments to the individual items so that your statement represents reality. For example, some of your income may not be shown at its frill amount, due to some bartering, thus it should be increased. Likewise, you may run many "extra" expenses, such as your automobile, gas, and insurance expense through your business statement. These expenses should be adjusted downward to show the "true" expenses.

C. VALUE THE TANGIBLE ASSETS OF THE PRACTICE

The tangible assets in your business are most likely completely depreciated yet in fact they do have a market value. These items should be valued as a conservative accountant would value them: in other words be reasonable. For instance, a computer that sold for $3,000 just a few years ago may now be down to about $500. The Buyer is going to know this. You do not want to negotiate over the value of fixed assets when you have an offer, it is much better to negotiate over the potential growth of your practice.

D. SET A VALUE FOR THE PRACTICE

You should take into account the three most used appraisal techniques: 1) Market comparison.; 2) Discounted future earnings, and 3) Cost of reproduction. These methods are discussed in detail in Business Brokerage, Inc.'s Report: How to Value Your Accounting Practice.

1) Market Comparison approach

The Market Comparison approach directly compares the subject practice with sales of similar practices. The basic principal underlying the market comparison approach is substitution; a Buyer would not pay more for a practice than the cost of a substitute practice of equal utility and desirability. This is considered the most accurate of all value indicators if there is adequate data available and the subject properties are somewhat homogeneous. Since there are approximately 30,000 public accounting practitioners in California, there are obviously many sales transactions. However, since public recordings are not required, it is very difficult to obtain accurate data. Buyers and Sellers generally will not give you much information, and at most, it will definitely not be the complete story.

The Rule-of-Thumb is a derivation of the Market Comparison approach. When, after making many appraisals of similar businesses, the indicated value generally is about the same as some ratio (such as X month's gross revenue. X year's gross revenue. X month's net profit, X week's deliveries, X percent of sales, X percent of cost, etc.) Then, often, people in the industry develop a rule-of-thumb as a shortcut to estimating an approximate value.

COMMENT: Business Brokerage has many years of involvement in accounting and tax practice sales, and thus, has an extensive database of all their past sales. Being active in statewide sales, we are also "in-tune" with current trends and regional differences in practice values.

2) Discounted cash flow earnings approach

The discounted cash is the present value of a future stream of cash flows, which is established by discounting those flows by a percentage rate that reflects cost of capital and opportunity cost elements. To determine a fair price for an acquisition candidate by means of the discounted cash flow concept, you need to know (1) the cash flow, (2) the period over which to measure it (the conventional measuring period is ten years), and (3) the terminal value (a concept designed to reflect the theoretically perpetual cash flows, here calculated by taking the presumed amount for which the company can be sold at the end of Year 10 under some definable criterion, such as a certain P/E ratio, a function of a certain number of years cash flow, or book value). The discounted cash flow method of appraisal is a derivation of the IRS Excess Earnings method of appraisal, but emphasizes future estimated performance rather than past performance.

3) Cost of reproduction approach.

The cost of reproduction (also called Replacement Cost) approach is an asset-oriented method of estimating value. This approach is also based on the principle of substitution, i.e., a Buyer would not pay more for the subject property than it would cost him to duplicate the property by assembling all of the individual components of the subject property. In the case of an accounting practice, the Buyer would consider the cost of renting an office, furnishing the office, hiring staff, implementing a marketing program to acquire client, and factoring in an amount for working capital to last until the cash flow develops.

The cost of reproduction approach is most useful in appraising a primarily asset-based business such as a machine shop and is least useful in a service-based business such as an accounting practice. However, an accounting practice Buyer will always have in mind the thought of "going it by himself" and starting his own practice. This is especially true if the Buyer is a "marketing oriented" type of individual. And, it is exactly this type of individual that is usually the most successful in the purchase of a practice.

E. PREPARE A PROSPECTUS

The prospectus that you prepare should be both an informational report and a piece of sales literature at the same time. Remember that while it is important to present all of the facts about your practice to the Buyer, it is also important to provide opinions as to how the features of your practice will provide benefits to the Buyer. While some of these benefits may seem obvious to you, it may not be so obvious to the Buyer. Thus, you should figuratively hold him by the hand and walk him through your practice via the prospectus, pointing out all of the facts, features and benefits he will acquire.

COMMENT: Business Brokerage has been preparing a sales prospectus for accounting practices for many years. Buyers comment frequently that our report is excellent in that it provides a tremendous amount of information in an easy to read format. This saves everyone's time. And, it sells a lot of practices!

F. ADVERTISE WIDELY YET CONFIDENTIALLY

Question: How do you get the word out that your practice is for sale, yet, keep the sales efforts confidential from your employees, clients, competitors and creditors? Some use a blind P.O. Box or File Number in a professional journal. Of course, confidentiality is one of the major advantages of using Business Brokerage, not only for advertising but also for handling all of the inquiries with discretion.

While you may get a good response from putting out the word locally, you will maximize your chances of getting the best deal by exposing your practice to the entire marketplace. This way you are more likely to find someone that will take over your lease, purchase your furniture and equipment, and have the wherewithal to meet your terms.

COMMENT: The majority of our Sellers of accounting practices over the last decade chose out-of-town Buyers, even though we advertised to the town where the practice was located as well as to accountants from the entire state. In fact, in a survey of our 1990 sales, we found that 77.7% of the Buyers were from out of town, 33.3% were from different counties, and the average distance between the Buyer and Seller was 49.9 miles.

G. HANDLE INQUIRIES, QUALIFY BUYERS (see Buyer Scorecard in Appendix)

While you will probably receive many inquiries for your practice, you will have to carefully screen for the Buyer that meets your requirements. Many of the Buyers will say they are very serious about making a purchase quickly. However, you will find that they are ready to make a move on unrealistic terms, such as: no down payment, 20% earn-out plans, trial purchase agreements, etc. There will be corporate controllers that have money for the down payment but little or no practical production-oriented experience. There will be practitioners with ample experience in their own practices, but will not pay top dollar. There will be young, well educated, but unseasoned Buyers without substantial assets accumulated for a large down payment. You must be sure to ask the difficult questions needed to get to the "quick" and avoid wasting your time.

H. CONDUCT INTERVIEWS

1) Confidentiality. Just to be sure, have your Buyer sign an Agreement of Confidentiality. You must protect your client list and the systems that you have created over the years.

2) Get the Buyer to Talk. Ask the Buyer what kind of practice he has and what he is looking for in a practice. Objective: to determine the Buyer's motivation and to get him to start talking about himself and his practice. He will tell you exactly what he has and wants so that you can tell him how your practice will satisfy his wants.

3) Handling Books and Records. The Buyer will probably ask to see your books, records, IRS returns, etc. Tell him that these items are confidential until an offer is on the table with a good faith deposit.

4) Handling Client Files. You should show the Buyer an example of 1 or 2 tax and write-up files as an example of your' work. Tell him the remaining files are confidential until an offer is on the table and you have accepted it.

5) Handling Price and Terms. When the Buyer gets around to the price and terms (even if he has already seen them in your prospectus), tell him what you think is a fair price, but also tell him that you would look at any reasonable offer.

6) Closing: Credibility & Getting Realistic. You must be sure that the Buyer is totally convinced that what you have told him is the truth. All Buyers come in very skeptical and must be slowly shown that you have what you say you have.

Frequently, Buyers have attended one of the no money down seminars. They want to offer you a payback as a percentage of the gross revenue that they receive over 5 years, (effectively transferring all of the business risk to you). It is my opinion (and the market bears this out) that practices are very difficult to build and that your practice is definitely worth a handsome sum of money. We sell almost all of our practices in a range of 100% to 125% of one year's gross revenue plus the market value of the furniture and equipment. We always get a sizable down payment (or sometimes a smaller down payment, but with real estate as collateral). It is important that the Buyer have some money at stake to ensure that he will give your practice the utmost attention.

7) Don't Waste Time with Projections. Buyers often ask the Seller to prepare elaborate projections or ledgers of past client's fees, etc. You can easily spend 10 or more hours to find the Buyer only offers you 50% on the dollar for your practice. Don't waste your time. If you have given the Buyer good and sufficient information on your prospectus so that he can make an intelligent offer, then he is too interested in minutiae to ever make it in private practice. You will also be exposing yourself to a lawsuit if the projections do not materialize.

8) Encouraging Offers. The best position that you can be in as a Seller is to have Buyers bidding on your practice. To get offers, however, you must ask for them. This is where most Sellers fall down and a good salesman earns his keep.

I. HANDLE OFFERS AND NEGOTIATIONS

1) Reading between the lines of an offer. Always look for the downside of an offer and the person associated with the offer. Go through an exhaustive list of "what ifs" to be sure you cover all of the potential situations that could occur in the future.

2) Analyzing the Buyer's risk tolerance. In the purchase and operation of any business, there are inherent risks, even to the point of the road being torn up in front of your office for 3 months. Does the Buyer seem to be the type of person that can handle the risk by looking for solutions rather than blaming the Seller, the economy, and the clients for any setbacks?

3) Long haul safety or short-term squeeze. Can the Buyer handle the terms of his offer if there is a downturn in gross revenues? If your deal's repayment structure doesn't leave room for contingencies, you may end up with a destroyed practice back on your hands. You might want to consider creating a win-win situation where you will get the maximum return over the entire length of the agreement.

4) Selecting the best deal. Will the Buyer's personality mesh with your clients? Does the Buyer bring experience and talents in certain areas that will benefit the clients and increase gross? Will the Buyer be interested in making the practice grow? Will the

Buyer have your clients' interest at heart? In the long haul, service to clients is what makes any practice successful. Be sure that your Buyer is so oriented.

5) Countering. This is often one of the most delicate areas of any negotiation. If you make a counter to one of the terms and it is not accepted, how do you reverse yourself without giving a sense of backing down or weakness (assuming the counter was to a non-deal breaking point)?

This is perhaps the one best reason to use Business Brokerage for third party negotiation techniques. As a third party, it is easy for us to send up trial balloons, to ask questions and find out the Buyer's real agenda.

6) Keeping the others alive while waiting for the winning offer to come through. Another delicate area. You can often get the best deal if you end up with multiple offers on your practice. But, you can also alienate the Buyers and end up with a lousy deal, another area where a third party can maintain the interest in your practice.

7) Due Diligence: Form over substance. If your practice paperwork is in good order, your Buyer's investigation will go well. Best if you lay out a "road map" of your practice so the Buyer can readily follow the cash flow and make a few checks.

J. DOCUMENTATION (See Appendix)

Paperwork protects your legal rights and documents the trail of events leading up to the final agreement. Be sure to get all terms and conditions in writing. Seems obvious doesn't it? Then why do we get frequent calls from Buyers, Sellers and attorneys to offer opinions and interpretations on do-it-yourself deals and other broker's deals?

Here is a list of documents, filings, and agreements that you will want to cover.

1) Buyer's Scorecard (Appendix FORM A- 1)

2) Agreement of Confidentiality (Appendix FORM A-2)

3) Declaration of Satisfaction and Waiver of Contingencies (Appendix FORM A-3)

4) Credit Check (Appendix FORM A-4)

5) Agreement for Sale of Assets (Appendix FORM A-5)

   a. Lease or lease assignment

   b. Promissory note(s)

c. Security agreement

d. Exhibits: Furniture & equipment, client list, etc.

e. Covenant not to compete

f. UCC filings

g. Corporate Resolution

h. Trust Deed

IV. APPENDIX:

Following are some forms that you may find useful in selling your accounting practice.

FORM A-1

BUYER SCORECARD

A confidential guide to rating the potential Buyer(s) for a practice purchase. These traits and conditions have been shown to be the most likely causes and reasons for success or failure of small businesses.

Rating for ________________________________by_____________________________

Condition or Trait Score 1-5	Score
1. Financial Strength	
a) Capacity to repay debt	______
b) Adequate reserves-working capital	______
c) Adequate capitalization	______
2. Managerial Competence	
a) Knowledge	______
b) Experience	______
c) Marketing	______
d) Administration	______
e) Recordation, organization, planning.	______
3. Personality Characteristics	
a) Drive/energy-persistence, initiative, health	______
b) Thinking ability: creative, analytical	______
c) Communication ability: oral, written	______
d) Human relations: considerate, cheerful, cooperative, tactful	______
e) Flexibility: accept and adapt to change.	______
TOTAL SCORE (65 possible)	______

Excerpted from Small Business Research Series No. 2 "The First Two Years", and Small Business Research Series No. 4 "Personality and Success," both published by the Small Business Administration. Business Brokerage, Inc. makes no representations or warranties regarding the accuracy or completeness or predictability of the information contained herein. Any Seller must rely entirely upon his/her own investigation and judgment.

FORM A-2

CONFIDENTIAL DISCLOSURE AGREEMENT

THIS AGREEMENT made and entered into as of the _______day of ___________, 20__ by and between ____ having its principal place of business at ___________________________ (hereinafter referred to as Buyer") and ____ , having its principal place of business at _________________________________ (hereinafter referred to as "Seller").

WITNESSETH

Whereas Buyer desires to obtain certain confidential and proprietary information from Seller for the sole purpose of determining if Buyer will purchase the Seller's business, and

Whereas Seller is willing to provide such confidential and proprietary information to Buyer for the limited purpose and under the terms and conditions set forth herein.

Now, therefore, in consideration of the mutual covenants and promises set forth herein, the parties hereto agree as follows: 1. DEFINITIONS. "CONFIDENTIAL INFORMATION" as used herein shall mean all customer lists, client files and all other information, documentation, and software (including listing thereof and documentation related thereto) disclosed or made available by Seller to Buyer, including, but not limited to the existence of discussions between Buyer and Seller, and Seller's business plans, present and future products, and policies; 2. ACKNOWLEDGMENT. Buyer acknowledges and agrees that CONFIDENTIAL INFORMATION is proprietary to and a valuable trade secret of Seller and that any disclosure or unauthorized use thereof will cause irreparable harm and loss to Seller; 3. OBLIGATIONS OF Buyer. In consideration of the disclosure to Buyer of CONFIDENTIAL INFORMATION, Buyer agrees to treat CONFIDENTIAL INFORMATION in confidence and to undertake the following additional obligations with respect thereto: (a) to use CONFIDENTIAL INFORMATION for the purpose of determining if Buyer will purchase business of Seller; (b) not to copy, in whole or in part, CONFIDENTIAL INFORMATION; (c) not to disclose

CONFIDENTIAL INFORMATION outside of Buyer's firm; (d) to limit dissemination of CONFIDENTIAL INFORMATION to only those of Buyer's employees who have a need to know to perform the limited tasks set forth in Item (a) above; and (e) to return CONFIDENTIAL INFORMATION, including all copies and records thereof to Seller upon receipt of request therefor from Seller, or a decision by Buyer not to purchase business of Seller, whichever occurs first; 4. SURVIVAL. The restrictions and obligations of Paragraph 3 of this Agreement shall survive any expiration, termination or cancellation of this Agreement and shall continue to bind Buyer, its successors, heirs and assigns; 5. NEGATION OF LICENSES. No rights or licenses, expressed or implied, are hereby granted to Buyer under any patents, copyrights or trade secrets of Seller as a result of or related to this Agreement; 6. GOVERNING LAW. This Agreement shall be construed and enforced in accordance with the laws of the State of California. In witness whereof the parties hereto have caused this Agreement to be executed by their duly authorized representatives.

______________________________	______________________________
______________________________	______________________________
Seller (s)	Buyer (s)

FORM A-3

REQUEST FOR A TRANS-UNION, EXPERIAN, OR EQUIFAX CREDIT REPORT

Dear Sirs: Please send me a copy of my credit report. I have enclosed $15.00 for this report.

Full Name:____

Spouse:____

Street Address:____

City:___________________________ State: ________ Zip:_____________________

Years at this address:___________ If less than 5 years at above address, indicate prior addresses for last 5 years below:

Street Address: ____

City:____________________________ State: ___________ Zip:__________________

Years at this address: ____

Street Address: ____

City: ___________________________ State: ______________ Zip:________________

Years at this address: ____

Birth date: _____________ SSN#: __________________ Month Year: _____________

Signature: _________________________________ Telephone: _________________

FORM A-4

DECLARATION OF SATISFACTION AND WAIVER OF CONTINGENCIES

BUSINESS ______________________________

ADDRESS ______________________________

PHONE ______________________________

HOME ______________________________

In connection with the Offer to Purchase Agreement with respect to the above-described business, the undersigned Buyer declares that he or she has made an independent investigation of said business and hereby declares his/her complete satisfaction of any and all contingencies as contained in the Offer to Purchase Agreement. Buyer has personally inspected this business and is satisfied that he or she has the ability to conduct same. Also, Buyer has checked the Seller's financial statements, books and records, and hereby approves same.

Additionally, Buyer specifically has examined and approves each of the following:

_____ Financial Statements, books & records, customer lists/files.

_____ Lease and/or assignment thereof.

_____ Premises, fixtures, equipment, appliances, computers, software are in good condition and in working order.

_____ Other (if none state, none) ____

____

_____ Buyer agrees to maintain fire and theft insurance to cover the assets of the business as of the date of transfer. The insurance policy shall set forth the Seller as first loss payee.

Executed on ____________________20___ at ____________________ California

Dated _________________________ 20___

____

Buyer

FORM A-5

AGREEMENT FOR SALE OF ASSETS (Outline)

RECITALS

1. Scope of Agreement.

2(a) Guarantee.

2(b) Seller's Rights to Refer New Business.

3. Purchase of Assets.

4. Purchase Price.

5(a) Inventory of Furniture, Fixtures and Equipment.

5(b) Sales Tax on Furniture, Fixtures and Equipment.

6. Location of Business.

7(a) Prorations of Expenses.

7(b) Prorations of Work in Progress.

7(c) Prorations of Retainer Fees Paid in Advance.

7(d) Accounts Receivable.

7(e) Assumption of Subscriptions/Contracts.

8. Covenant Not to Compete.

9. Transfer Date.

10. Allocation of Purchase Price.

11. Warranties and Indemnification of Seller.

12. Miscellaneous Provisions.

13. Severability

14. Time is of the Essence.

15. Mandatory Arbitration.

16. Brokerage Fees.

17. Alienation.

18. Assignment and Successors.

19. Additional Documents.

20. Warranties and Representations of Buyer.

21. Notices.

22. Confidentiality.

23. Compliance Storage.

24. Contract Services of Seller.

25. Promissory Note(s).

26. Security Agreement.

27. Assignment of Lease.

28. Corporate Resolution.

FORM A-6
ADDENDUM TO WILL

You may want to sign the following statement and put this report with your will

BEING OF LEGAL AGE AND SOUND AND DISPOSING MIND AND MEMORY AND NOT ACTING UNDER FRAUD, MENACE, DURESS OR UNDUE INFLUENCE OF ANY PERSON OR PERSONS WHOMSOEVER DO MAKE, PUBLISH AND DECLARE THAT IN THE EVENT OF MY TERMINAL ILLNESS, INCAPACITATION OR DEATH, IMMEDIATELY CALL BUSINESS BROKERAGE, INC. TO LIST MY PRACTICE WITH THEIR FIRM. THE FULL PRICE SHOULD BE APPROXIMATELY_____ TIMES LAST YEAR'S GROSS REVENUES. THE DOWN PAYMENT SHOULD BE APPROXIMATELY______% WITH THE BALANCE OF THE PURCHASE PRICE PAID OVER ____ YEARS. THERE SHOULD BE AN ADJUSTMENT OF THE FULL PRICE AT THE END OF THE FIRST YEAR FOR ANY BUSINESS LOST.

SIGNED _____________________________ DATE ___________________________

V. REFERENCE SOURCES

BUSINESS BROKERAGE, INC. BIBLIOGRAPHY

BUSINESS PRINCIPLES

Covey, Stephen R. The 7 Habits of Highly Effective People. Simon and Schuster.
This is an excellent book that really describes the way we should all live both personally and professionally. Good reading and filled with examples. Emphasizes living and working within correct principles.

Girard, Joe. How To Sell Anything to Anybody. New York: Simon and Schuster.
An excellent first book about selling principles that every accountant should have. The author was the number one automobile salesman in the USA year after year. His sales were all one on one (not fleet sales). His story of climbing from failure to success is inspiring. This book is about the fundamentals of selling that apply to all products and services.

Mackay, Harvey. Swim with the Sharks. New York: William Morrow and Company, Inc.
An excellent source of ideas built on a lifetime of experience by a businessman that is involved in life and business. Easy to read. A book that you can open up to any page and get a one or two page idea with an example that can help you immediately.

Peter, Manna J. and Waterman, Jr., Robert H. In Search of Excellence. New York: Warner Books.
Principles of running a company learned by studying the most successful companies in America. These are principles that an accountant should know and be able to pass on to clients to improve their clients' business.

Peters, Tom and Austin, Nancy. A Passion for Excellence. New York: Warner Books, Inc. 1985.

What do the most successful Companies in America all have in common? A passion for excellence. Excellence in product, customer service, management of workers, etc. Another Tom Peters book that really covers the subject and provides lessons for accountants as well as good ideas that can be passed on to clients.

Pickle, Hal B. Personality and Success. Washington, D.C: Small Business Administration. 1964.

This 84 page booklet is part of the author's work for his degree of Doctor of Philosophy in Business Administration at the University of Arkansas. The book is the result of his study of the primary factors of success and failure by businessmen in operating their small businesses. The factors studied were: drive, thinking ability, human relations ability, communications ability, and technical knowledge. Written in 1964, but just as valid today.

Ringer, Robert J. Winning Through Intimidation. California: Los Angeles Book Publishers Co.

One of my favorite books, really not about intimidation, but rather about lessons learned in real life concerning "how not to get taken in business" and "working smart instead of hard." Easy and amusing to read.

Ringer. Robert A. Million Dollar Habits. New York: Fawcett Crest Book. 1990.

Easy read with good advice about sound life and business principles. Filled with amusing anecdotes from real life.

Von Oech, Roger, Ph.D. A Whack on the Side of the Head. New York: Warner Books.

"Discovery consists of looking at the same thing as everyone else and thinking something different." This is the thrust of the book, breaking the 10 mental locks and seeking

answers not obvious at first. Author has a very wry sense of humor. The book is filled with metaphors.

<u>BUYING OR SELLING A BUSINESS</u>

Baron, MBA, Paul B. <u>When You Buy or Sell a Company</u>. Connecticut: Center for Business Information, Inc.

A relatively complete book on buying, valuing and selling a business. The author writes in the first person and adds many anecdotes. A lot of interesting information, but not really a guide in the sense of offering forms, examples, etc.

Goldstein, Arnold S. <u>The Complete Guide to Buying and Selling a Business.</u> Mentor.

Written by an attorney/business broker/professor. Good general guide to finding and buying a business. Covers locating a business, pros and cons of franchising, where to obtain financing and negotiating techniques. Appendix contains sample letter of intent, agreement for sale of assets, stock sale/redemption agreement and franchise agreement.

Ryan, Charles R. <u>Cashing in Your Chips.</u> Illinois: Flow Jones-Irvin.

Written by an independent management and valuation consultant to business and professional practices. Book is concerned with accounting for all of the money you have invested into a business and developing an exit strategy to maximize your return in taking your money out of the business. Includes chapter on advantages and disadvantages of different ownership structures when selling out your business.

Scharf, Charles A. and Shea, Edward E. and Beck, George C. <u>Acquisitions, Mergers, Sales, Buyouts and Takeovers.</u> New Jersey: Prentice-Hall, Inc.

Written by Charles Scharf, a practicing attorney involved in mergers and acquisitions and a lecturer for seminars and universities. Edward Shea is an attorney and general counsel to GAF Corporation and a Professor at Pace University. George Beck is an attorney involved in business combinations, mergers, divestitures and securities law. This is a graduate-school level textbook covering mergers and acquisitions of public companies.

Contains one of the most complete checklists for a Buyer I have ever seen (pgs. 93-130) and also a complete sample acquisition contract with explanations of all clauses.

Valiulis, Anthony C. Covenants Not To Compete: Forms, Tactics, and the Law. Wiley Law Publications.

This book provides the legal history and legal cites for covenants not to compete between employers and employees and between Buyers and Sellers. Included is a state by state case digest appendix.

NEGOTIATION

Cohen, Herb. You Can Negotiate Anything. New Jersey: Lyle Stuart Inc.

A general text book-like approach to the art of negotiation.

Fisher, Roger and Ury, William. Getting to Yes. Penguin Books.

Roger Fisher teaches negotiation at Harvard Law School, was the originator of the popular television show "The Advocate," and is the Director of the Harvard Negotiation Project. William Ury is a consultant, writer and lecturer on negotiation and mediation and is Associate Director of the Harvard Negotiation Project. This book is a concise step-by-step strategy for coming to mutually acceptable agreements. It is based on studies and conferences of the Harvard Negotiation Project, a group that deals continually with all levels of conflict resolution.

<u>Document created by: DAVID C. SMITH, Business Brokerage, Inc. Founder</u>

Resume:

PROFESSIONAL EXPERIENCE:

BUSINESS BROKERAGE, INC., is involved in appraising, listing, marketing, arranging financing and selling of practices throughout California. Firm has sold over 1,400 practices worth over $160,000,000 to date. Licensed Real Estate Broker in California.

SOUTHLAND BUSINESS SALES, Anaheim, Ca. 1973 to 1976. Agent for a business broker selling liquor stores, machine shops, restaurants and service businesses.

MERRILL LYNCH, Newport Beach, Ca. 1971 to 1973. Stockbroker

EDUCATION:

David Smith received his BS degree in Finance from California State University at Long Beach. He also has an AA degree in Real Estate from Santa Ana College and has taken undergraduate studies at Indiana University. Mr. Smith has completed several courses in financial planning.

David Smith has attended numerous courses and seminars including: APPRAISING CLOSELY HELD BUSINESSES and BUSINESS VALUATION FOR ACCOUNTANTS presented by The Institute of Business Appraisers; MERGERS AND

ACQUISITIONS OF MID-SIZE BUSINESSES by Darrel Fouts, Colorado Business Consultants; BUYING AND SELLING BUSINESS OPPORTUNITIES by Wilfred Tetreault, American Business Consultants.

Mr. Smith has presented seminars on Valuation of Accounting and Tax Practices to the Orange County Society of CPA's (MAP committee), SFV EA's, Inland Society of Tax Preparers, San Diego Chapter of CSCPA's, the CSEA "Super Seminars" and many other professional groups.

Mr. Smith was also a major contributor to Valuing Small Businesses and Professional Practices by Dr. Shannon Pratt, Dow Jones-Irwin, Homewood, Illinois.

David Smith hails from Birmingham, Michigan and after college and military service settled in Orange County, California.

RESUME OF LEE RIBOLIN, CALIFORNIA REAL ESTATE BROKER

PROFESSIONAL EXPERIENCE:

Lee is a graduate of the University of Maine with a B.S. in Business Administration with a concentration in Finance. Lee worked as an Agent for Business Brokerage, Inc. (BBI) for 7 years before leaving to join an International Technology Company.

Lee then started his own business in Atlanta, Georgia, which he operated successfully for 13 years.

Now, Lee has rejoined BBI as a Broker and brings a great deal of experience in operating a business. With 10 years experience with BBI, Lee is highly regarded by Sellers to find the best qualified Buyers andin completing sales transactions professionally and in the timeframe required by the Seller and Buyer. Lee currently is located in Northern California and manages California practices for sale in zip codes above 9360x (north of Paso Robles to the Oregon border.

Lee also has participated in events (seminars/conferences) for tax professionals held by Spidell Publishing, Inc. (Lynn Freer).

Lee is an avid cyclist, swimmer and enjoys travel.