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WILLIAMSON & WYATT



# Developing a Business Transition Plan

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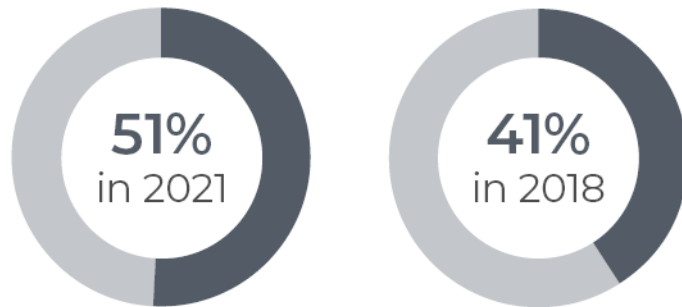
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2018 versus 2021

### Manufacturers with transition plans

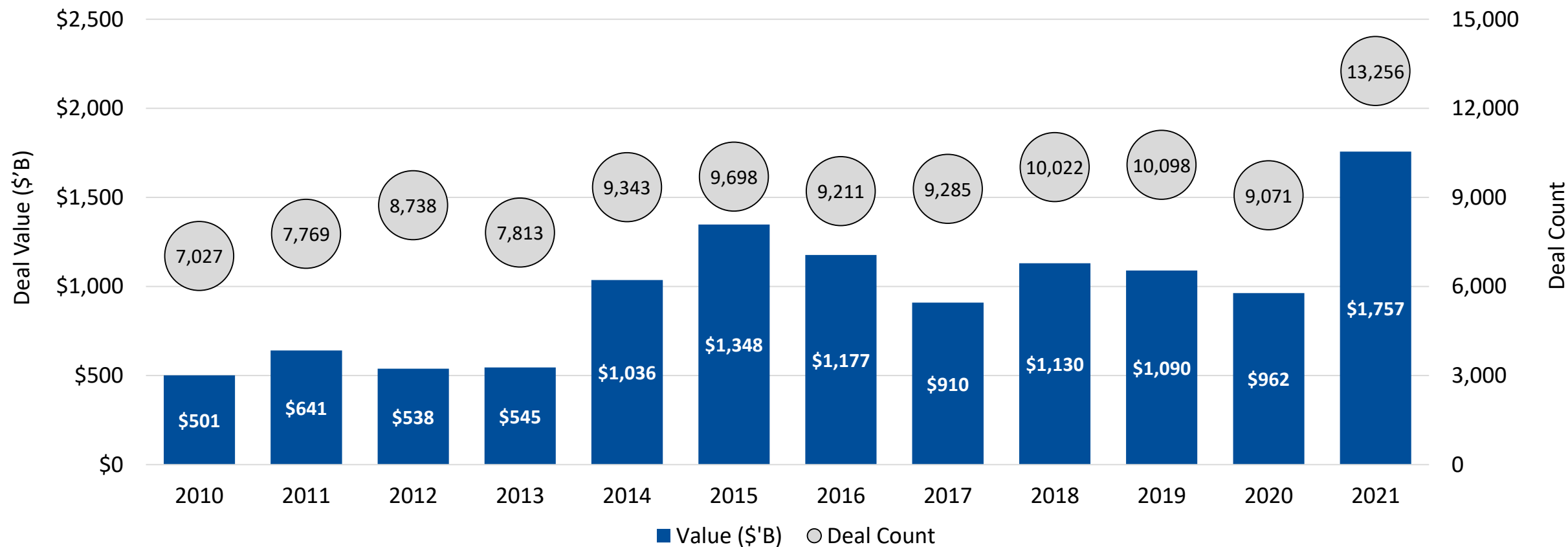


**6 out of 10 manufacturers**  
expect a transition within the next two years. An  
increase from four out of ten in 2018.



## Annual U.S. M&A Activity

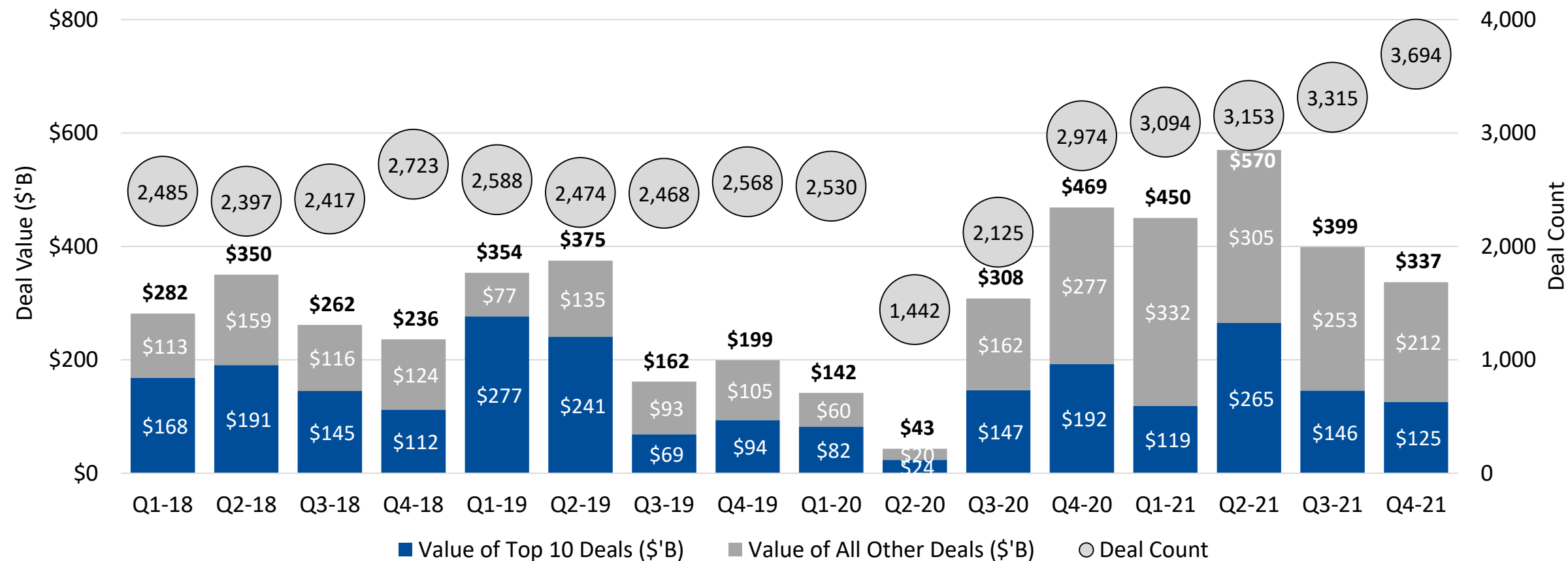
- 2021 set a record for M&A activity in the U.S. with 30% higher annual deal values and volumes than the previous highs set in 2015 and 2019, respectively



Source: S&P Capital IQ

# Quarterly U.S. M&A Activity

- Deal volumes continued to increase throughout the year in 2021 while deal values peaked in Q2 driven by the top two deals that represented nearly 30% of total deal value for the quarter



Source: S&P Capital IQ

- Uncertainty around tax rates
- Sidelined Capital
- COVID Fatigue
- Private Equity “Institutionalization of Everything”

# Manufacturing: Public Company Valuations

## Key Sector Considerations

### Reshoring Supply Chains

The COVID Pandemic has driven OEMs to reduce dependencies on outsourced manufacturing and reshore their supply chains closer to their base of operations and end-market customers

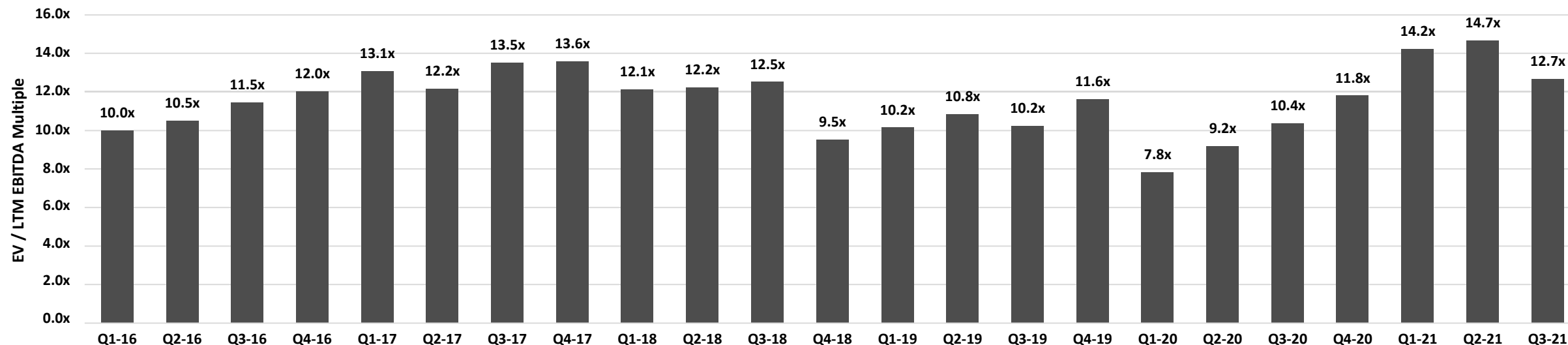
### Rising Input Cost Inflation

Surging demand for raw materials and labor amidst pandemic-induced supply chain disruptions has led to significantly elevated input costs

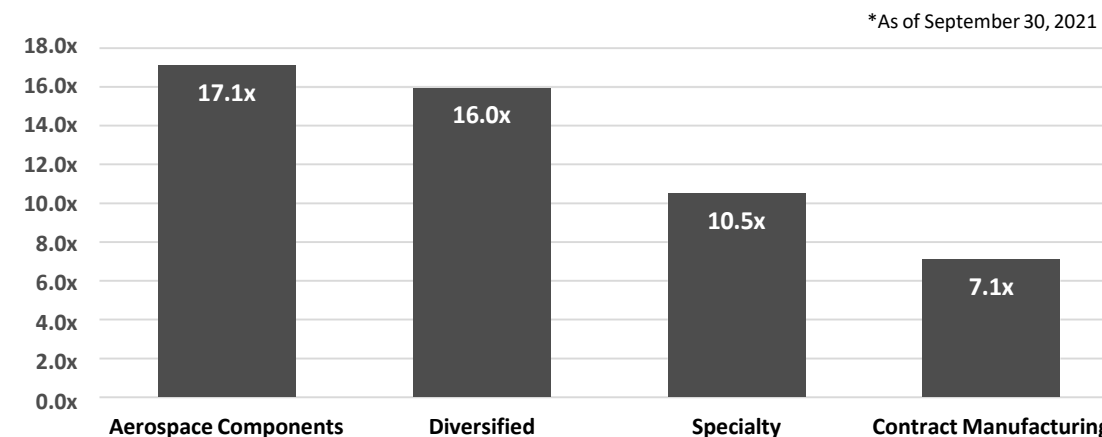
### Financial Buyers Drive Activity

Financial buyers set the pace for M&A activity in 2021 looking to acquire proprietary and mission-critical manufacturing capabilities through buy-and-build strategies

## Manufacturing Sector: Historical EV / EBITDA Multiples



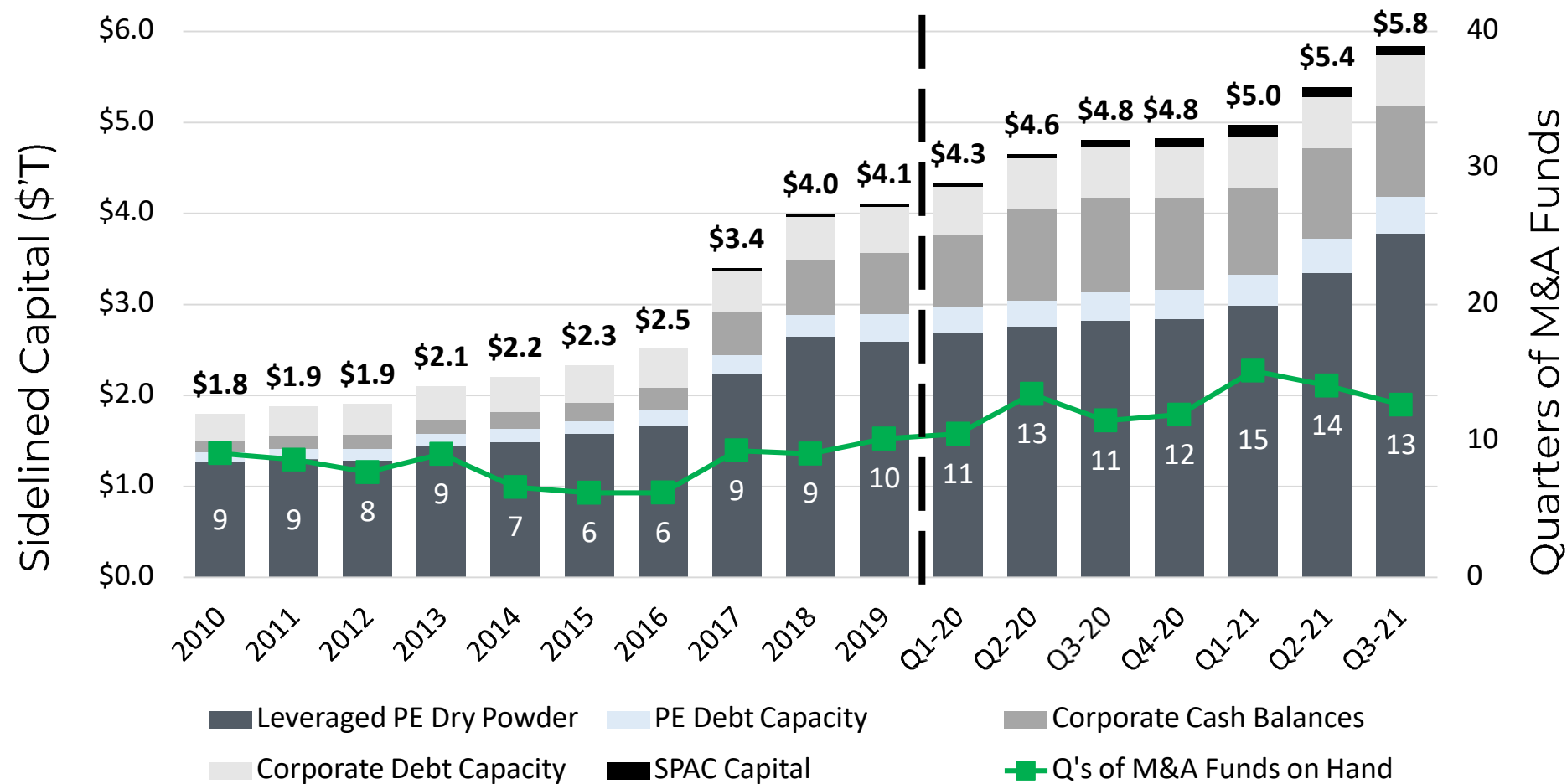
## Public Company EV / LTM EBITDA Median Multiples by Subsector



Private and Confidential Sources: S&P Capital IQ

# A Shortage of Attractive Targets Has Made Buyers More Anxious Than Ever Before

The capital available for M&A transactions currently totals 13 quarters of transactions. This backlog further intensifies the “seller’s market” as demand for transactions remains elevated



Note: Quarterly M&A Funds on Hand is based on the rolling four quarter average deal spend factored down by 25% for typical stock component.



# Is My Business Ready For a Sale Process? - Key Aspects of Seller Due Diligence

## Financial Forecast and Business Plan

- Need to have a three-year forecast that can withstand scrutiny
- Understanding sales by industry and key trends
- Understand the revenue opportunities and cost savings to the buyer

## Financial Statements

- Compliance with GAAP- Do you have an audit or review?
- Pro-forma financials that are free of one-time items and “owner costs”

## Key Contracts (e.g., customers, suppliers, and employment agreements)

- Watch out for change of control consents that grant undue leverage to third parties

## Operations

- What do you do that is special?
- What do you do that you know you can improve?

## People

- In-person will be held with the most interested parties

## Contingent Liabilities (e.g., environmental, guarantees, etc.)

## Intellectual Property (proper registration of trademarks and patents)

- Ensure the existence of employee invention and confidentiality agreements

### Typical Sellside Due Diligence Advisors

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Financial and Accounting

Tax

Legal

Environmental

Operational

IT

Market and Industry

## Internal Transitions

- Sale to Management or Key Employees
- Employee Stock Ownership Program
- Sale to Partner

## Third-Party Transitions

- Sale to Financial Buyer
- Sale to Strategic Buyer
- Joint Venture

## Transfer to Family Members

- Gift or sale to children

### **Intellectual Property**

(trade secrets, patents,  
trademark, copyrights)

### **Regulatory Risk**

(environmental,  
immigration, licensing)

### **Liability Risk**

(employees, ERISA,  
product liability, privacy)

### **Non-Compete Agreements**

## **Business Value**

### **Insurance**

(life, key-person, disability,  
health, E&O, liability)

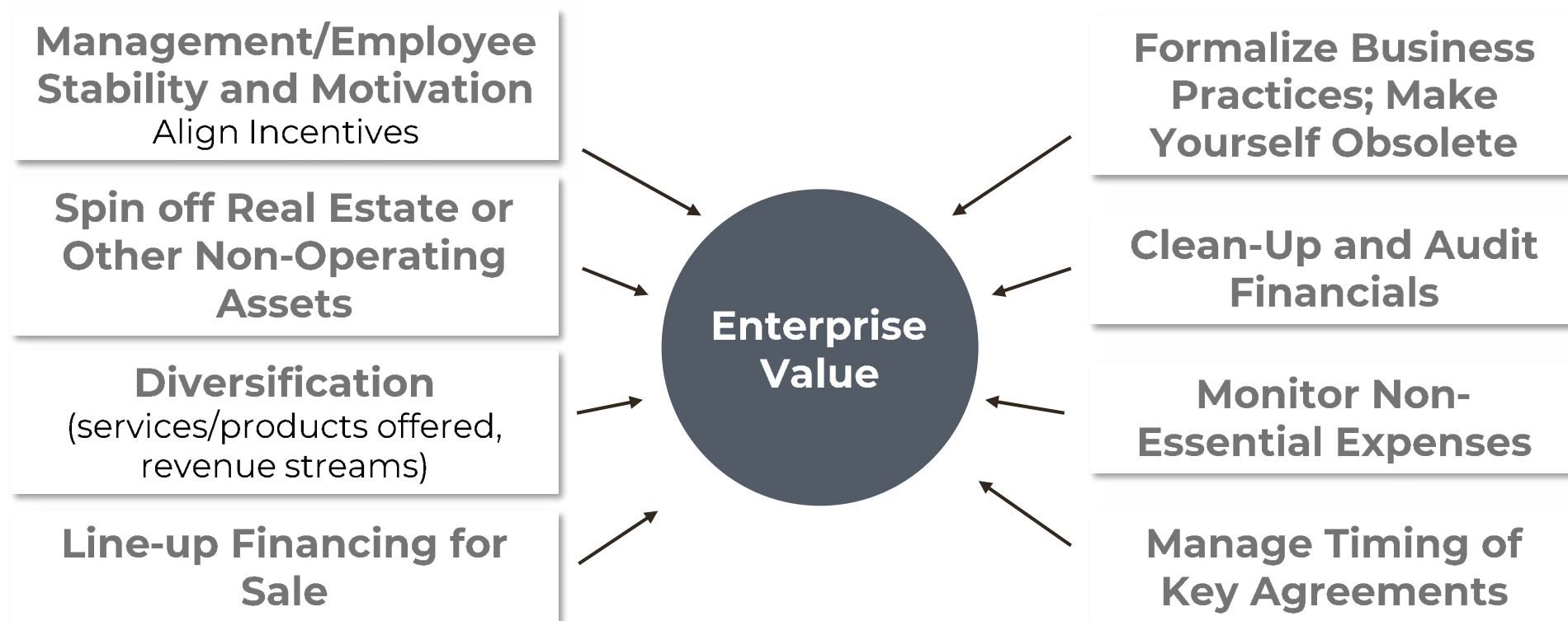
### **Contingency Plans**

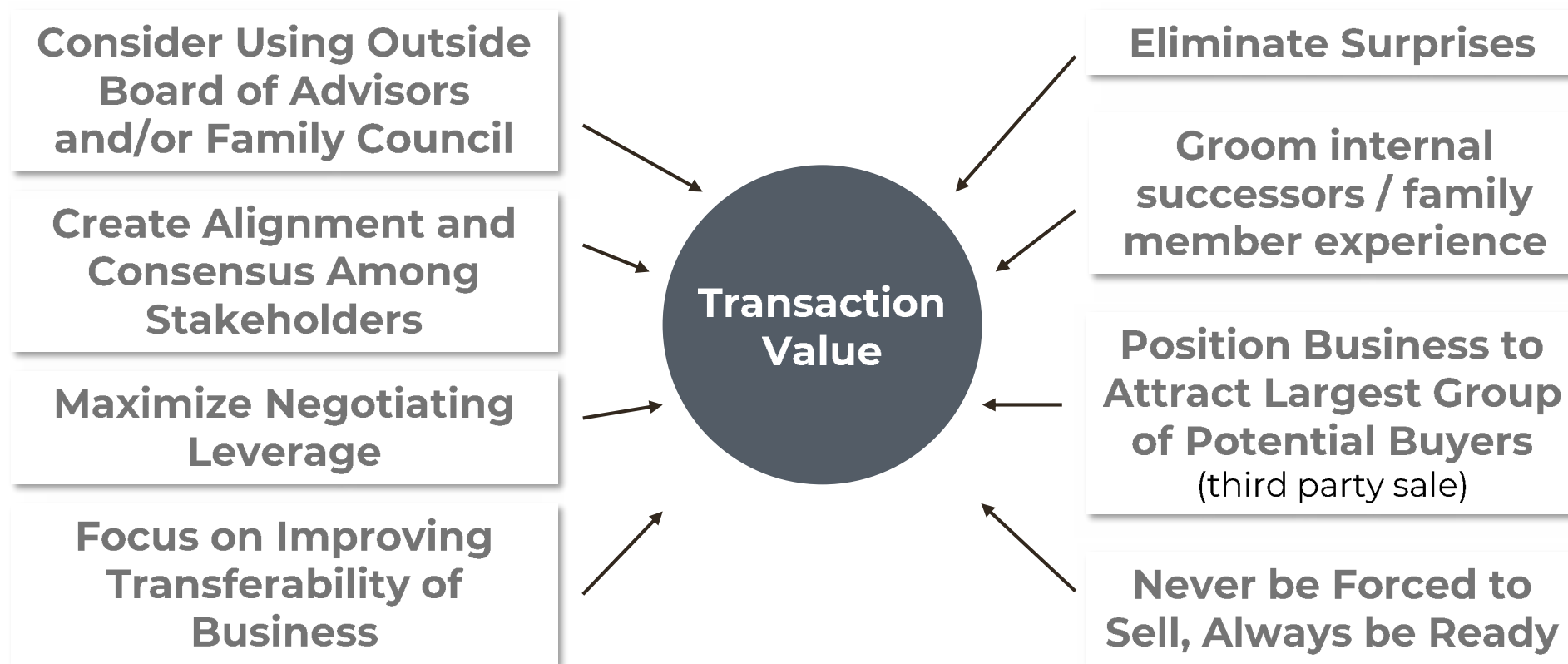
### **Clean up**

(Loose or Undocumented  
Agreements; Corporate  
Formalities)

### **Protect the Status Quo**

(access to credit, leases, key  
employees)





## Steps a Seller Can Take to Align Culture and Incentivize Continuity

- It is in the best interest of both parties – the buyer and the seller – to ensure continuity among key constituents and employees who have helped contribute to the success of the enterprise being sold
- Taking a proactive approach to assess cultural fit can mitigate risk and set the continuing enterprise up for success before the deal has even gone through

### Cultural Due Diligence

- Having an opportunity to meet a handful of prospective buyers and their broader teams helps sellers assess and understand the culture of different buyers
- Oftentimes, when cultures align, buyers become more enthusiastic about a transaction and may rise to the top of the bidding groups
- **A common procedure may also include speaking with the former principals of recently acquired companies to see how the company operated after the transition period**

### Cross-company Benefit Comparison

- Understanding the buyer's benefit and incentive programs is an important indicator of culture
- Most acquirers are very concerned with the retention and well being of key employee talent
- Work from home has increased the ability for companies to retain talent, even while rationalizing facilities
- **Joining a larger company can lead to upward mobility within an organization as the larger enterprise may have more opportunities throughout the organization**

### Employee Incentive Programs (Transaction and Continuity)

- Employee incentive programs come in all shapes and sizes
- Typically, these programs are designed to thank employees for their past service, incentivize continuity during and after the closing of a transaction, and provide financial stability to ease concerns of any changes post-transaction

## Employee Plans Typically Seen in a Transaction

	Transaction Bonus	Stay Bonus	Enhanced Severance
Timing of Payment	<ul style="list-style-type: none"> <li>Bonus paid at close</li> </ul>	<ul style="list-style-type: none"> <li>Typically bonus is paid 6-18 months after the closing</li> </ul>	<ul style="list-style-type: none"> <li>Commitment to pay specified severance amount if an employee is terminated post-close</li> </ul>
Typical Quantum	<ul style="list-style-type: none"> <li>25-100% of salary for transaction assistance only (more of a thank you)</li> <li>Often used to help modify equity plans in favor of an employee</li> </ul>	<ul style="list-style-type: none"> <li>25-100% of salary</li> </ul>	<ul style="list-style-type: none"> <li>6-12 months of pay</li> </ul>
Typical Use Cases	<ul style="list-style-type: none"> <li>Given to the controller or other highly utilized employee during the transaction who holds little equity</li> <li>Also used to thank certain employees</li> </ul>	<ul style="list-style-type: none"> <li>Used for key management that are important to the ongoing operations and valued by the buyers</li> </ul>	<ul style="list-style-type: none"> <li>Used for management important to ongoing operations, but value to the buyers is less clear</li> <li>Can be used for lower management instead of a stay bonus</li> </ul>
Communication to Employee	<ul style="list-style-type: none"> <li>A thank you for a successful transaction and the efforts leading up to it</li> </ul>	<ul style="list-style-type: none"> <li>You are valuable to us and the buyer, and we want to make sure you stick around</li> </ul>	<ul style="list-style-type: none"> <li>We don't think anything will happen, but if the buyer changes course, you are covered for a smooth landing</li> </ul>
View of the Buyer	<ul style="list-style-type: none"> <li>A cost to the seller, no ongoing value</li> </ul>	<ul style="list-style-type: none"> <li>If done properly, it would likely be a program the buyer would have also implemented</li> </ul>	<ul style="list-style-type: none"> <li>If at market, typically no material impact</li> <li>Can be a consideration for realizing synergies</li> </ul>
Cost to the Seller	<ul style="list-style-type: none"> <li>Full value less any tax benefits that can be captured</li> </ul>	<ul style="list-style-type: none"> <li>Depends; it can often be paid by the buyer (at least partially)</li> </ul>	<ul style="list-style-type: none"> <li>Generally no overt cost, but if it's too widespread, it may impact the bid</li> </ul>

*The plans above are not mutually exclusive; often a combination of methods can be used to reach the desired outcome*

A transition of business ownership will have a significant impact on your financial future. Start planning early.



### Personal Financial Plan

- Scenario modeling and stress testing assumptions
- Determining minimum net proceeds
- Lifestyle goals



### Family Gifting

- Completed gifts of shares or interest to other family members
- Leveraging gifts
- Updates to estate planning documents



### Philanthropic Giving

- Creating a family legacy
- Strategically select assets for charity