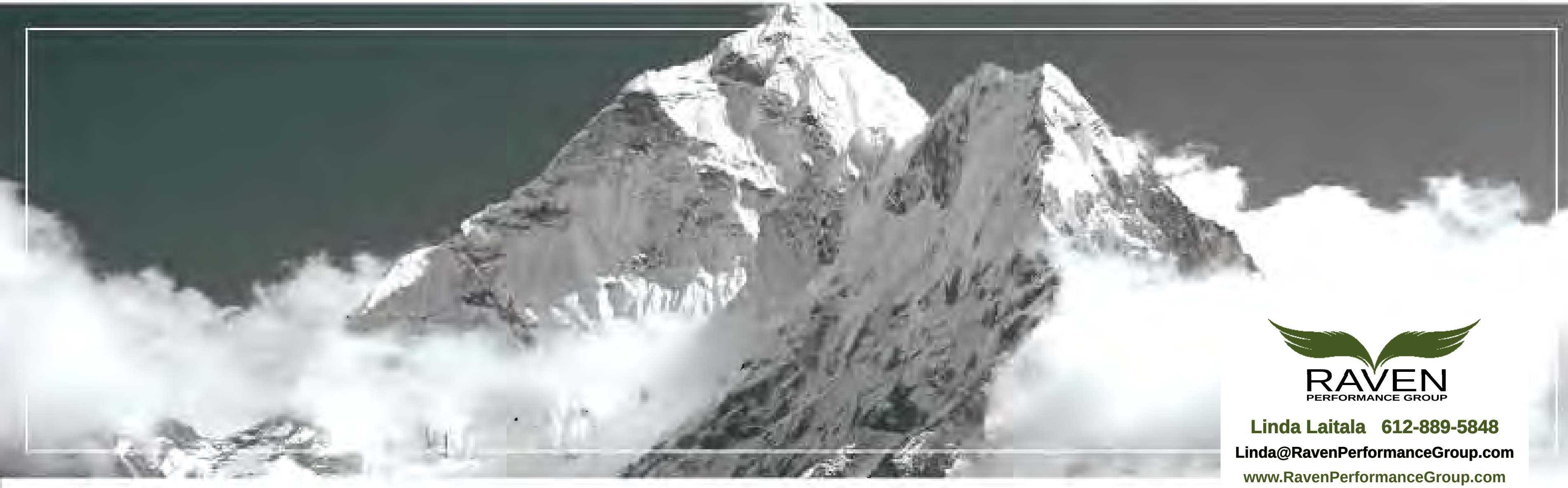

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EXIT PLANNING | Preparing, Valuing, Timing & Executing the Sale of a Business

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SUNBELT M&A GROUP

GRAY PLANT MOOTY

MINNESOTA SMALL BUSINESS DEVELOPMENT CENTERS Shaping the Future of Small Business

KDV WEALTH MANAGEMENT

RAVEN PERFORMANCE GROUP

INNER CIRCLE Better business. Richer life.

PANEL SPEAKERS

- **Paul Radeke – Financial Advisor, KDV Wealth Management, LLC**

  "How to Calculate the Funds Needed to Maintain the Desired Post-Closing lifestyle."

- **Barry Kirchoff – Director, Small Business Development Center, St. Cloud State University**

  "How to Prepare Your Business to Receive Maximum Value at the End of Sale."

- **Steve Kutscheid – Attorney-at-Law, Gray Plant Mooty**

  "The Sale Process – Economic, Legal, Psychological."

- **Dan Mulvaney – M&A Specialist, Sunbelt Business Advisors**

  "The Marketplace: Valuation, Transaction Structures and Buyer Expectations"

THE 3 CORE PLANNING PRINCIPLES

1 **TRANSITION FROM ASSET ACCUMULATION TO INCOME ALLOCATION**

Effectively transition your retirement savings accumulation strategies to distribution strategies.

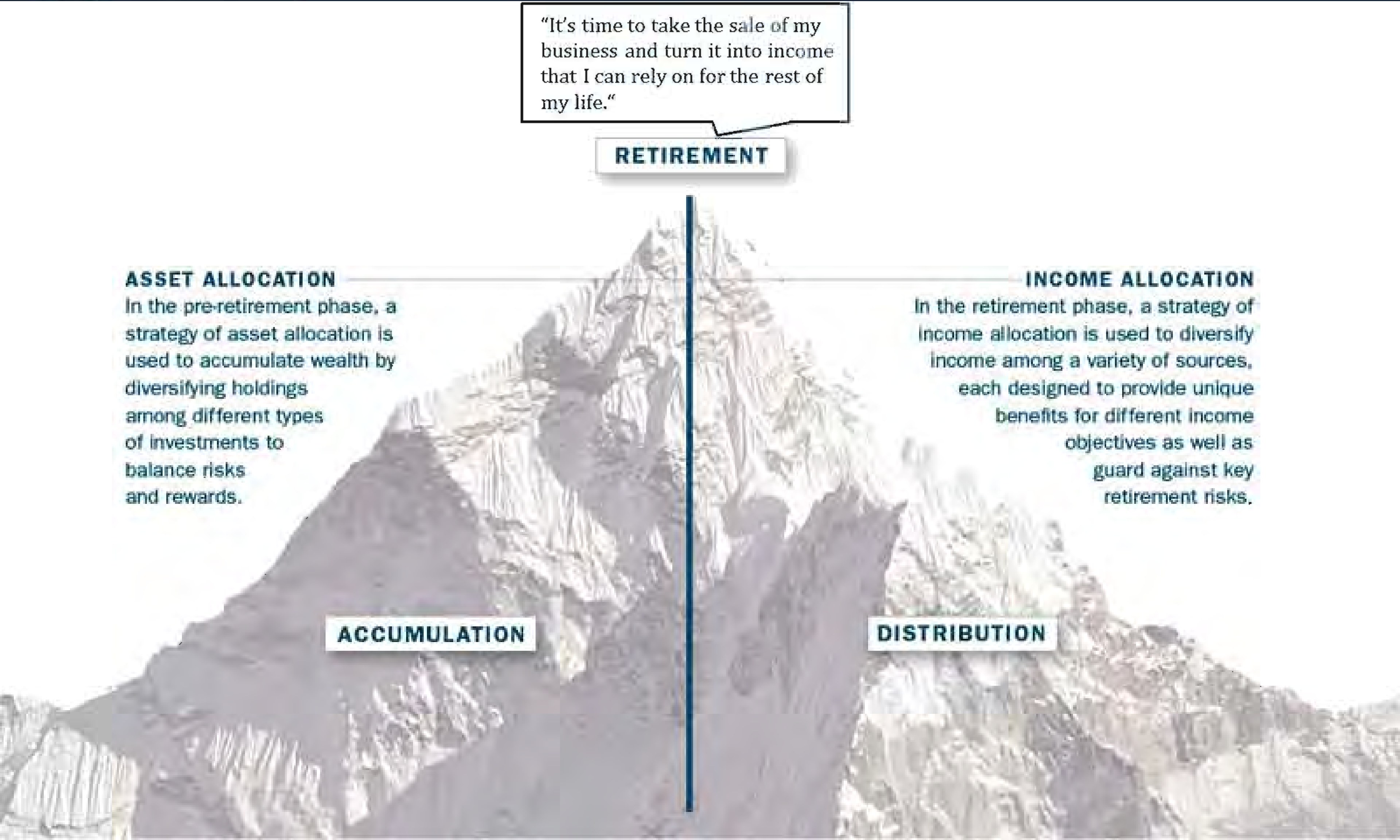
2 **DETERMINE YOUR WITHDRAWAL PERCENTAGE**

Determine the percentage of savings you can withdraw as income each year so it is sustainable *throughout* retirement.

3 **ADDRESS RISK**

Ensure that your annual income streams are protected against the key risks you will face during retirement.

THE GREAT TRANSITION



CALCULATING RETIREMENT INCOME

Top Down Approach

- Bureau of Labor Statistics' Consumer Expenditures Survey
  - Salary Range $60,000 - $90,000
  - 75%-89% of your pre-retirement income
  - Higher salary = lower replacement ratio

Salary	$100,000	100%
Minus current savings	($10,000)	10%
Minus payroll taxes	($7,650)	7.65%
Minus SS and Pensions	($10,000)	10%
Equals the wage replacement ratio	$72,350	72.35%

WITHDRAWAL RATE

- Table compares the different portfolios probability of funding retirements for 25 years.
- Careful evaluation of your asset allocation and initial withdrawal amount in retirement is vital.
- Each Initial withdrawal assumes a 3% inflation rate.

Initial Withdrawal Amount	25 – Year Retirement Stock / Bond Mix				
	100/0	80/20	60/40	40/60	20/80
3%	97%	99%	99%	99%	99%
4%	89%	93%	95%	98%	99%
5%	76%	79%	81%	82%	80%
6%	60%	61%	58%	50%	33%
7%	45%	42%	35%	22%	6%
8%	32%	27%	18%	7%	1%

CALCULATING RETIREMENT INCOME

Top Down Approach

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Minus SS and Pensions	($10,000)	10%
Equals the wage replacement ratio	$72,350	72.35%

$72,350 / 5% = $1,447,000 Portfolio Value

Calculating Retirement Income

Bottom Up Approach

- Within 5 years of retirement or contemplating a liquidation
- Establish your retirement goals
- Budget using current expense levels as a basis
- Full cash flow analysis

- The most comprehensive and accurate

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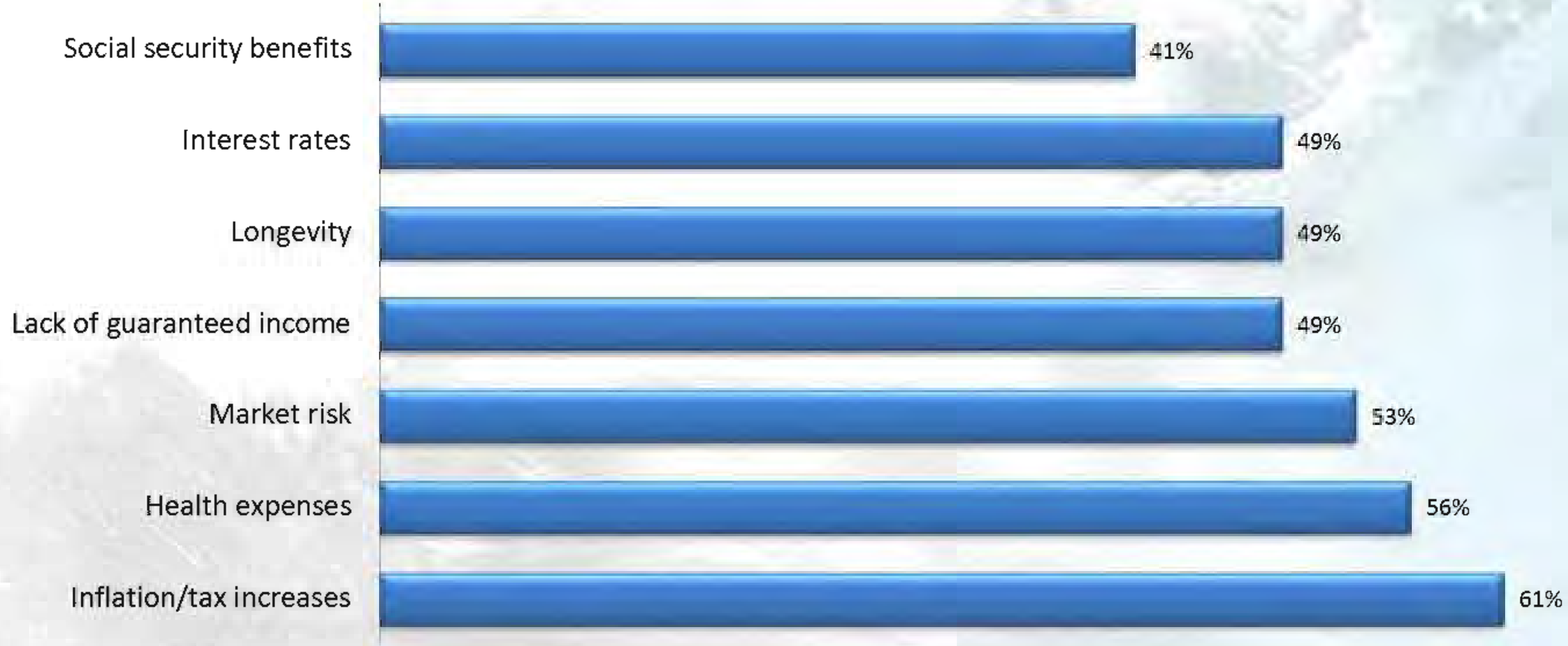
KEY RISKS OF RETIREMENT

Retirement survival requires the following risks to be addressed:

- Market
- Sequence of Return
- Longevity
- Health
- Inflation
- Liquidity
- Taxation
- Legacy

KEY RISKS OF RETIREMENT

Percent of consumers very or extremely anxious over specific retirement risks:

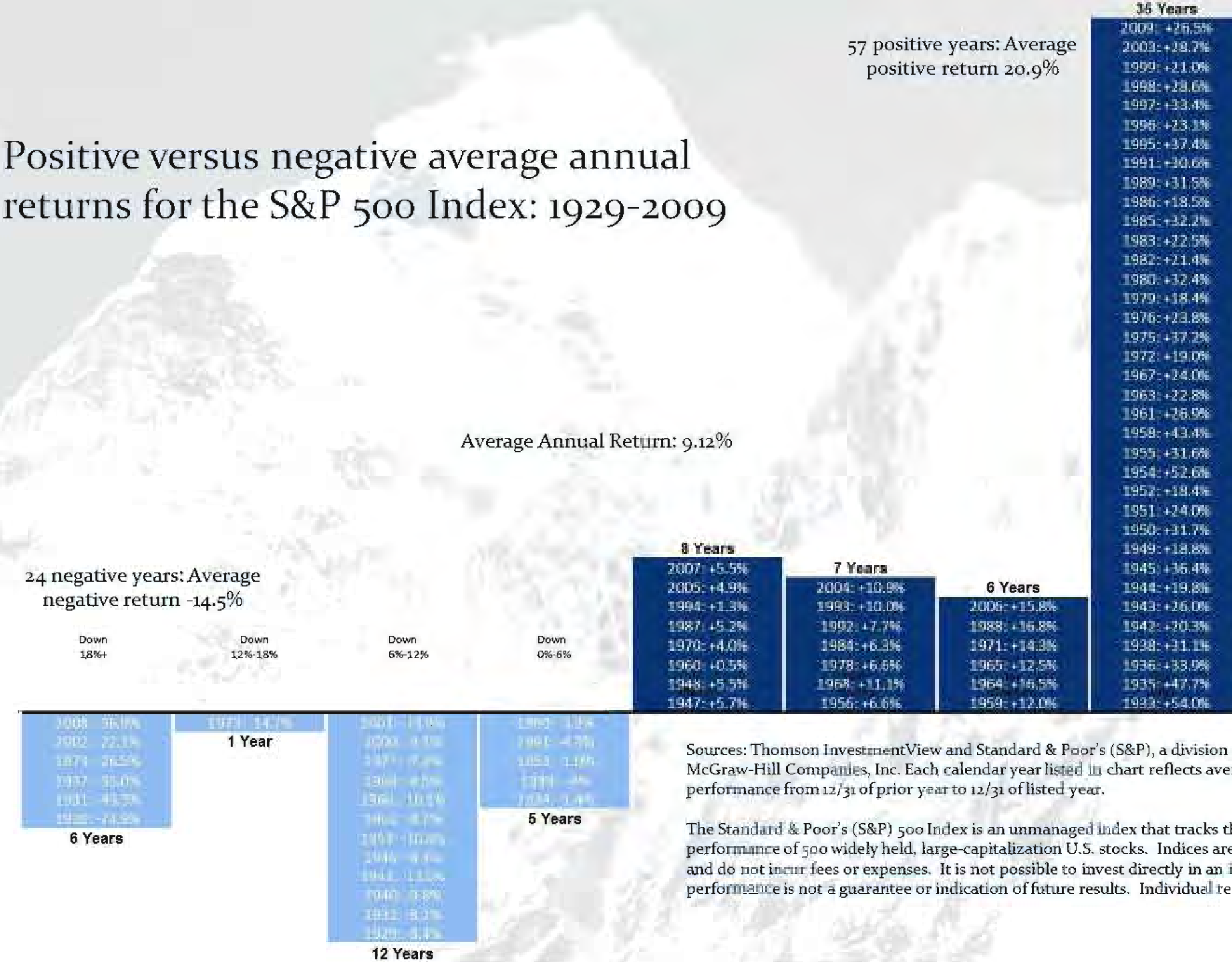


Source: McKinsey & Company 2007 Consumer Retirement Survey

MARKET RISK

MARKET RISK

Positive versus negative average annual returns for the S&P 500 Index: 1929-2009



Sources: Thomson InvestmentView and Standard & Poor's (S&P), a division of The McGraw-Hill Companies, Inc. Each calendar year listed in chart reflects average annual performance from 12/31 of prior year to 12/31 of listed year.

The Standard & Poor's (S&P) 500 Index is an unmanaged index that tracks the performance of 500 widely held, large-capitalization U.S. stocks. Indices are not managed and do not incur fees or expenses. It is not possible to invest directly in an index. Past performance is not a guarantee or indication of future results. Individual results may vary.

MARKET RISK

Equities – The Necessary Evil

- Equity exposure is typically needed to reach certain retirement objectives.
- Equities have historically been relied upon to be a powerful growth vehicle and inflation hedge.
- However, Market Risk, if not addressed, could wipe out your entire portfolio before or during retirement.

SEQUENCE OF RETURN RISK

SEQUENCE OF RETURN RISK

- It is not important when buying and holding (average returns work just fine for accumulation).
- Once you start withdrawing money in retirement (distribution), average returns are irrelevant.
- ***Example:*** *"If the market averaged 7% annually, I can safely assume that a 5% withdrawal rate is sustainable throughout retirement."*

SEQUENCE OF RETURN RISK

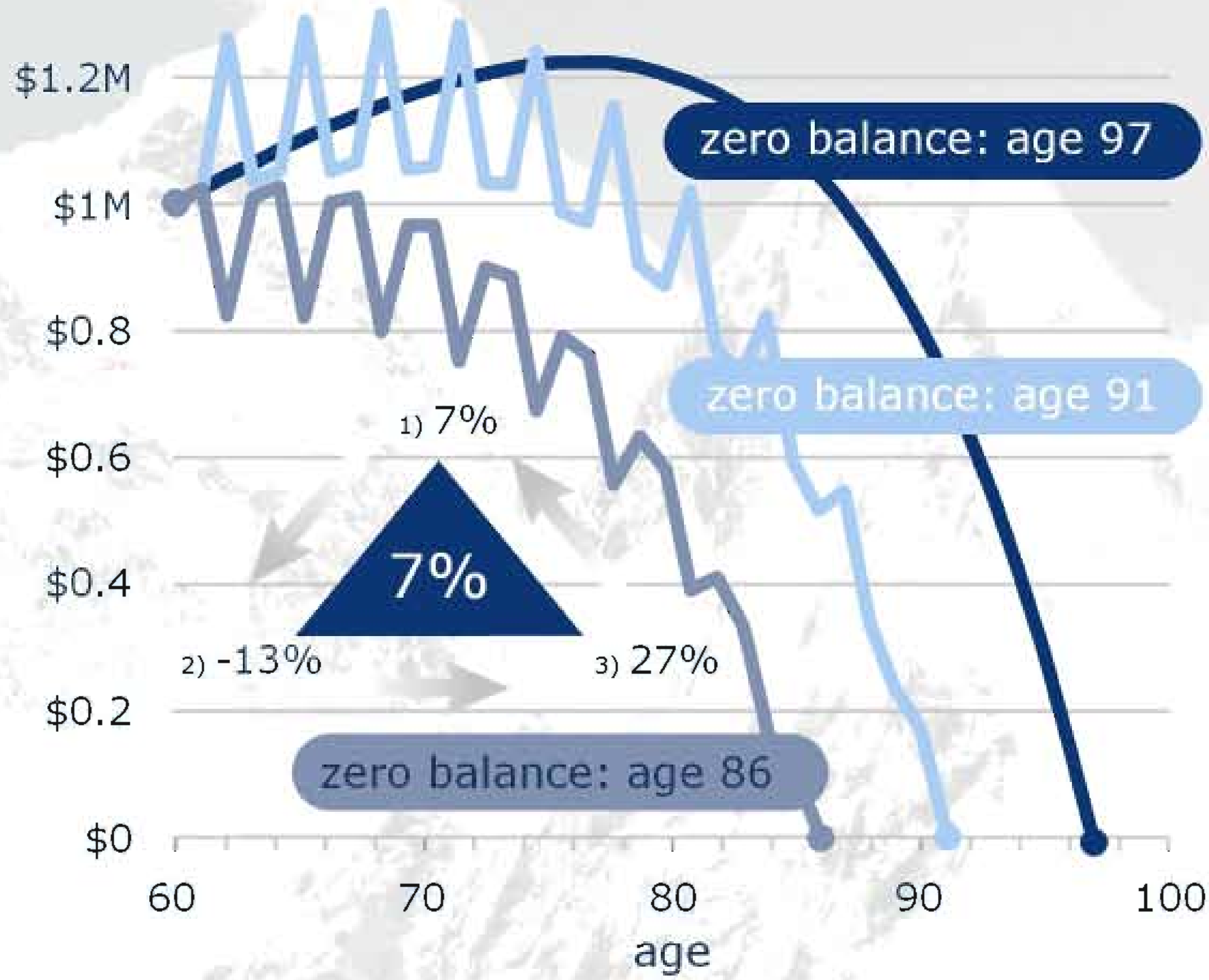
Hypothetical

Retirement age
60 years old

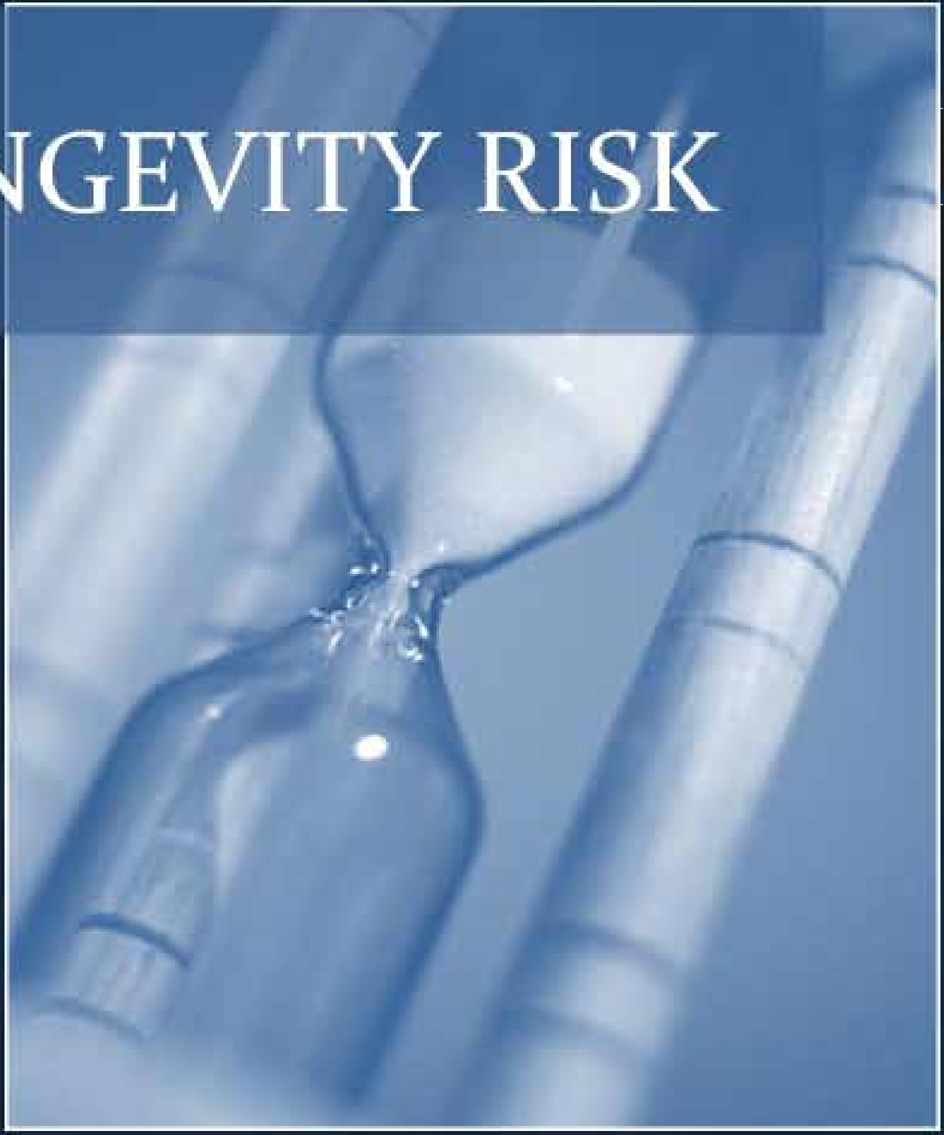
Investment
$1,000,000

Distributions
$50,000 every year,
increased annually for
3.5% inflation

This is a hypothetical example and is not intended to project the performance of any specific investment.



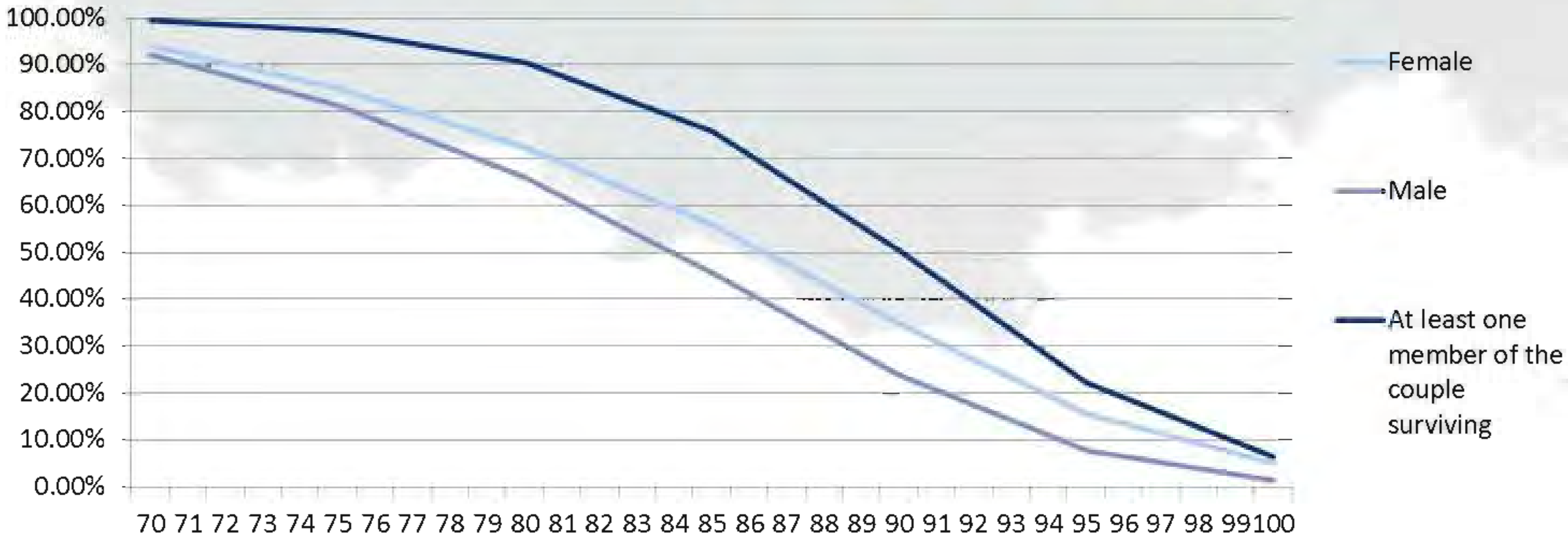
LONGEVITY RISK



LONGEVITY RISK

Probability of Survival at age 65

Age	Female	Male	At least one member of the couple surviving
70	93.90%	92.20%	99.50%
75	85%	81.30%	97.20%
80	72.30%	65.90%	90.60%
85	55.80%	45.50%	75.90%
90	34.80%	23.70%	50.30%
95	15.60%	7.70%	22.10%
100	5%	1.40%	6.30%



Source: RP2000 Mortality table; IFID Centre calculations

HEALTH RISK

HEALTH RISK

- Health care costs are growing twice as fast as general inflation.[1]
- 2 out of every 3 people age 65 and older will need some form of long term care in their lifetime.[2]
- Health care cost without long term care expenses is the second biggest expense for retirees, averaging about 20% of the couples total monthly expenses.[3]
- About 75 percent of single people and 50 percent of all couples spend all their savings within one year of entering a nursing home.[4]

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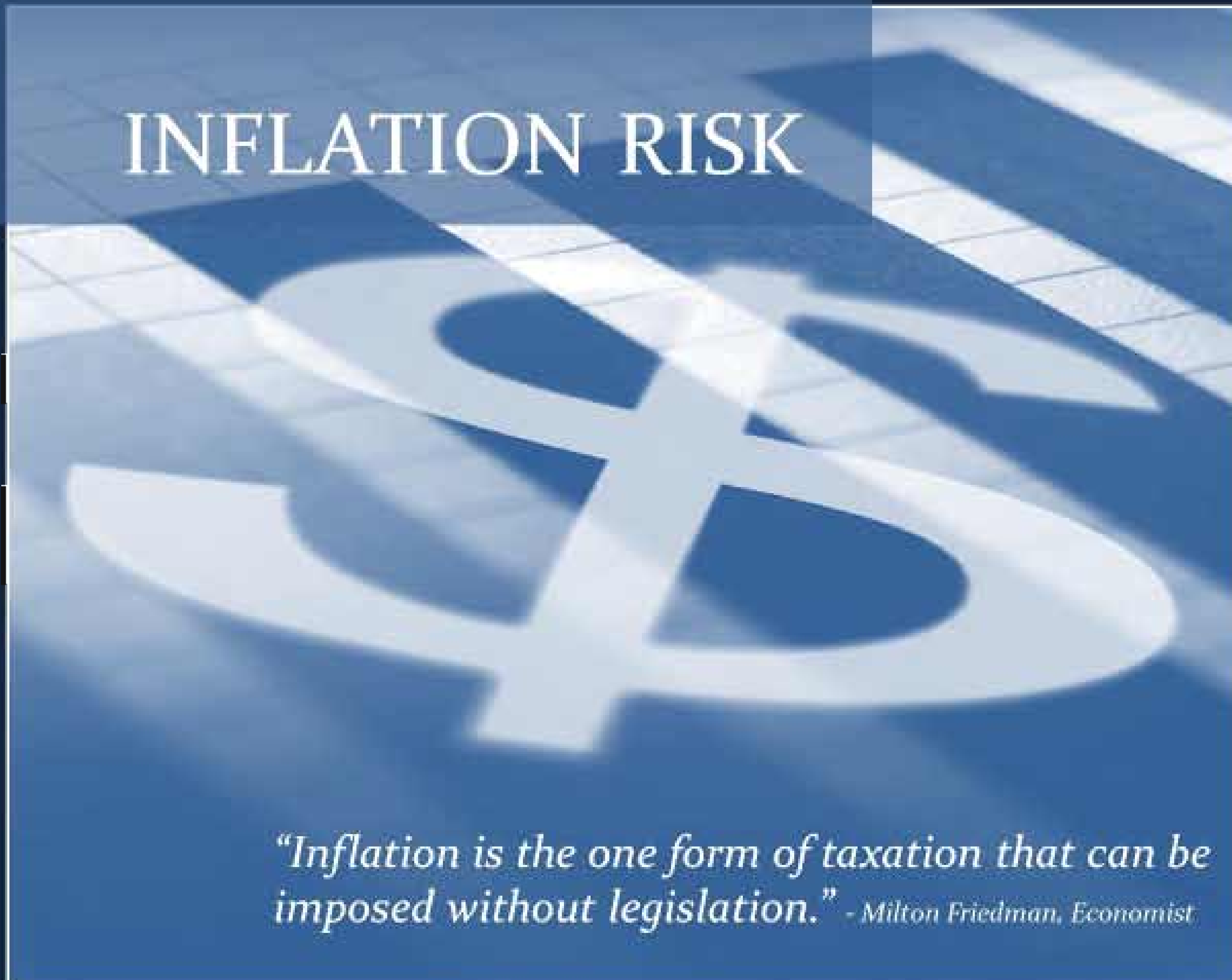
1 Fidelity, Investment News- Health-Care Expenses in Retirement Surge , March 13, 2006 .
2 "Americans Fail to Act on Long-Term Care Protection," The American Society on Aging, May 2003.
3 Are retirees' health costs as steep as some say? Market Watch, March 25, 2010
4 Long Term Care Insurance Tree ,September 2009.

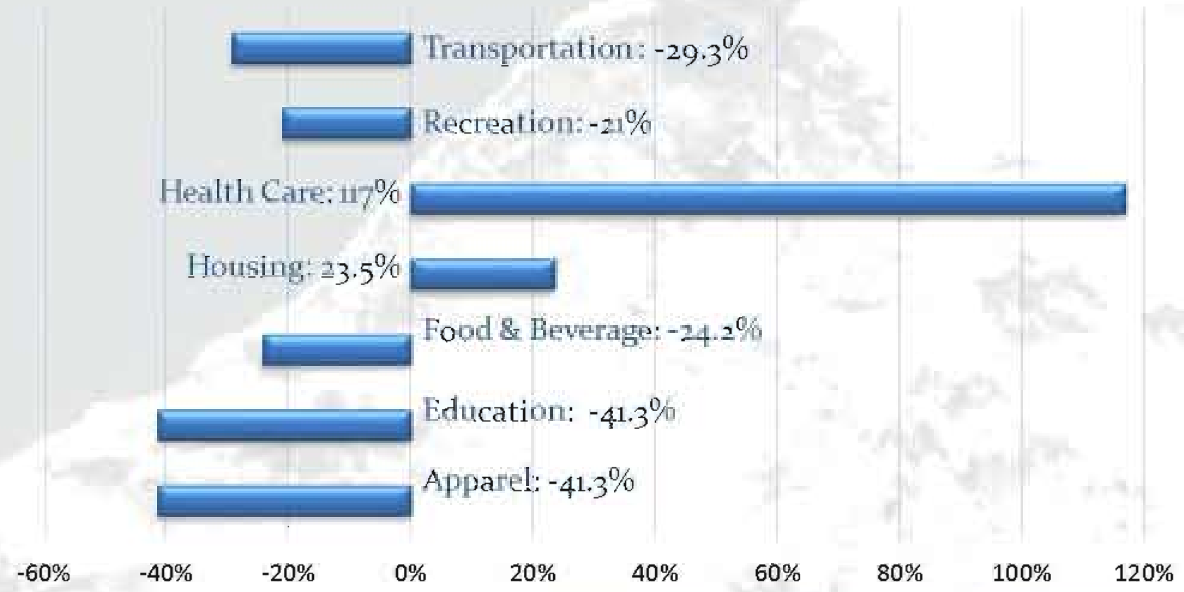

INFLATION RISK
"Inflation is the one form of taxation that can be imposed without legislation." - Milton Friedman, Economist

INFLATION RISK

- *"Inflation has superseded health care risk as the top concern of both retirees and pre-retirees. 58% are very or somewhat concerned and 71%, up from 63% percent in 2007, express concern that the value of their savings and investments might not keep pace with inflation."*

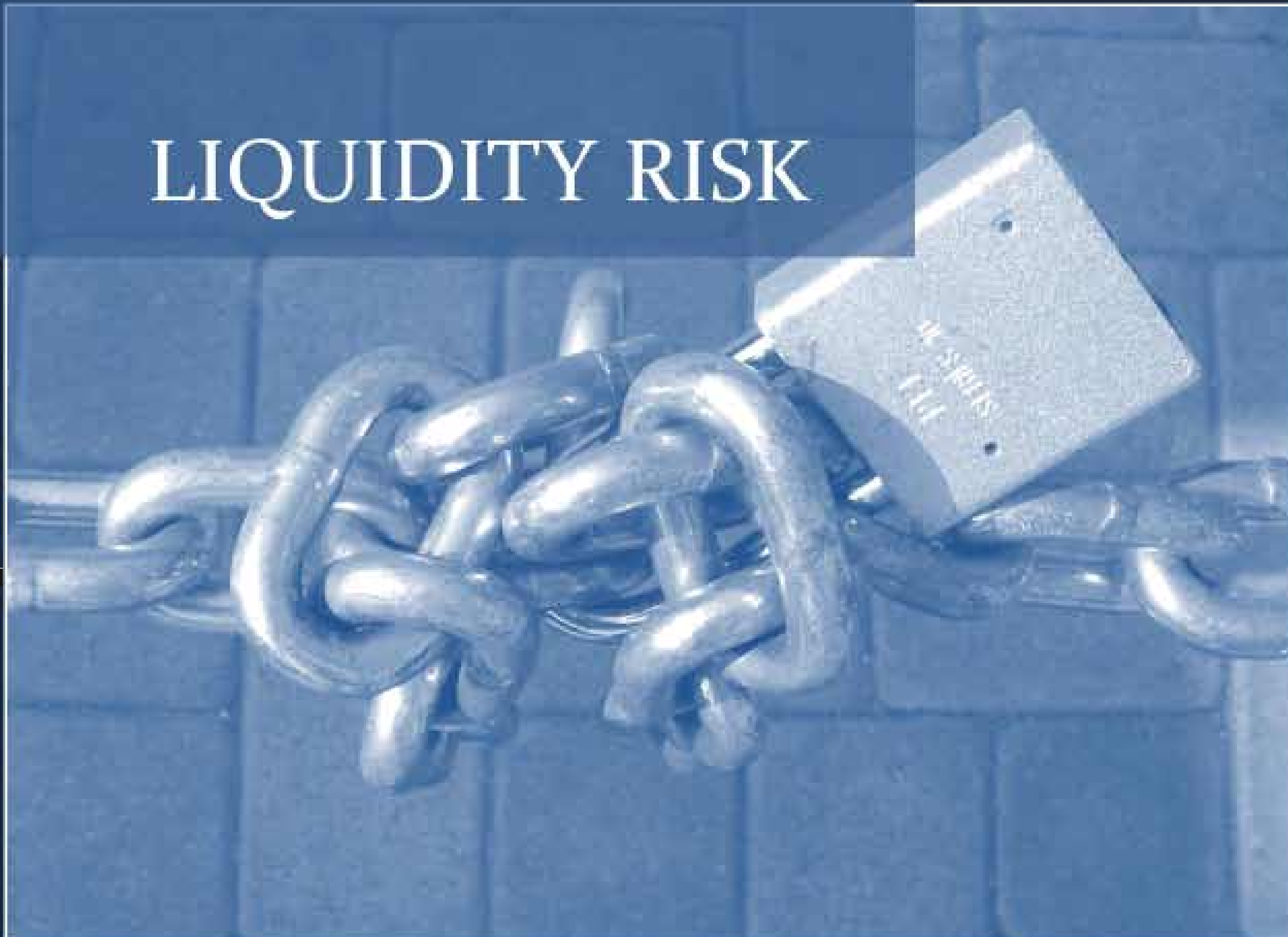
-2009 Risks & Process of Retirement Survey Report of Findings Sponsored by the Society of Actuaries (March, 2010)

- The Elderly Spend Differently:



Data Source: Bureau of Labor Statistics data to end of 2006; IFID Centre calculations

LIQUIDITY RISK



LIQUIDITY RISK

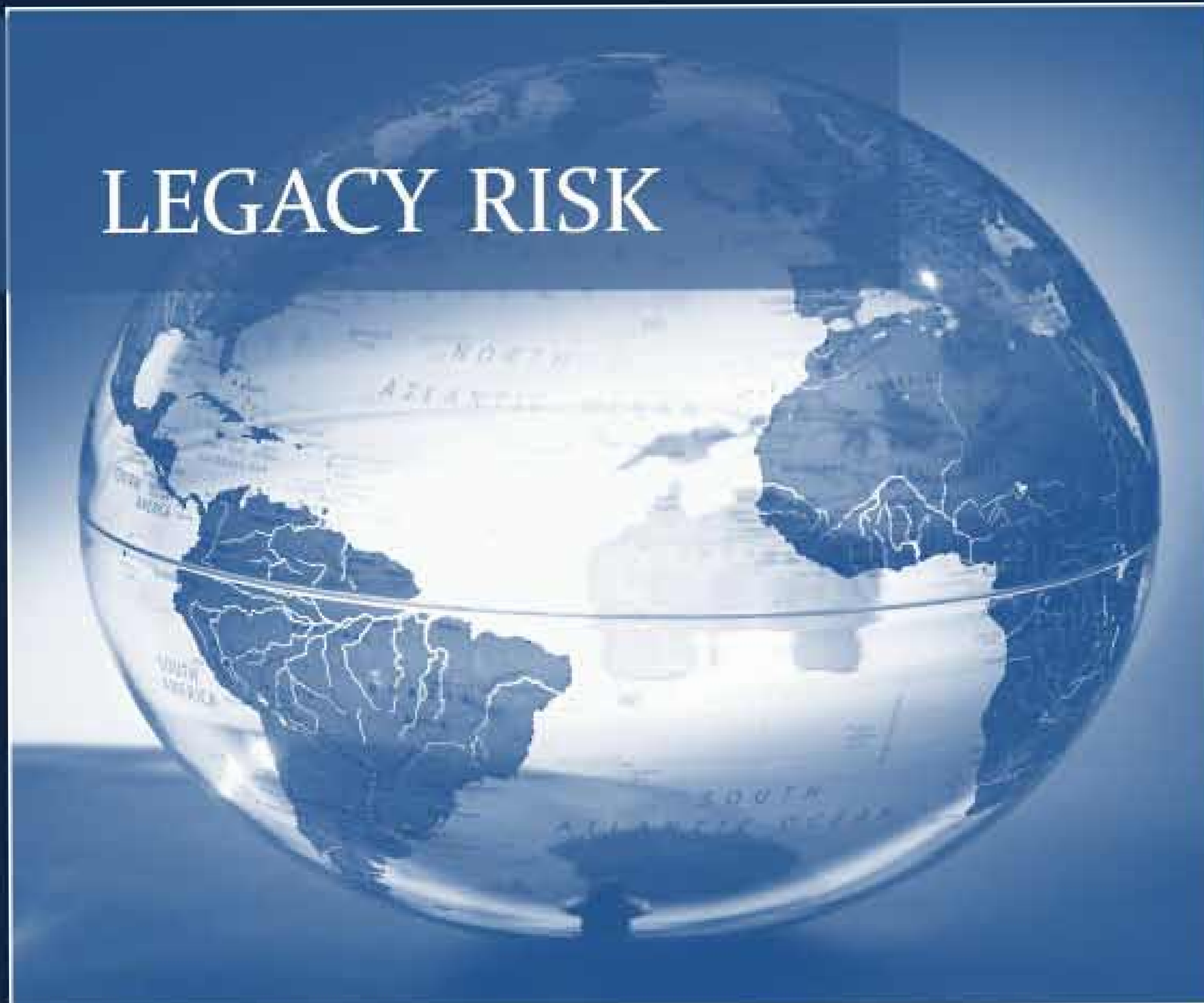
- Change is the one constant we can count on.
- Even the best retirement income planning strategy is vulnerable if flexibility is not incorporated to address unexpected events.
- Retirement has witnessed many “poor” millionaires.

TAXATION RISK

TAXATION RISK

- Taxation risk impacts the planning process for addressing the other key retirement risks
- The decisions we make today “eliminate” or “create” opportunities for mitigating taxes in the future

LEGACY RISK



VALUE DRIVERS

- Management Depth
- Customer Diversity
- Owner Involvement
- Competition.

VALUE DRIVERS

- Customer Satisfaction
- Human Capital
- Financial history
- Operating Efficiencies

Value Drivers

- Recurring revenue
- Professional Sense

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HOW TO PREPARE

- Seek Guidance from Professionals.
- Enhance or Develop Marketing, Financial, Operational Plans or Systems.
- Clean Up!

The Different Phases in the Business/Sale Process

THE LEGAL PROCESS

The Different Phases in the Business/Sale Process

I. Pre-Purchase Agreement Considerations & Documents
II. Structuring The Acquisition
III. Negotiating and Documenting the Purchase Agreement
IV. Buyer's Due Diligence
V. Closing

THE LEGAL PROCESS

I. Pre-Purchase Agreement Considerations & Documents

- Determine Owner's Objectives
- Build a Team of Competent Professionals
- Carefully Evaluate Enterprise Value of Business
  - Seller should never "Set the Price"
- Advance Resolution of Liabilities & Contingencies
- Resolve Legal Issues Relating to Key Assets
- Make sure "Key Employee" Agreements are in Place
- Use of Confidentiality Agreements

THE LEGAL PROCESS

- Use of Letters of Intent
  - Generally Non-Binding, but Make It Difficult to Renegotiate Terms
  - Creates a Moral Obligation on Sellers to Complete Transaction
  - May Prevent Sellers from Further Auctioning The Business
  - May Create Unwanted Publicity
  - Buyers Assume Sellers have Psychologically Committed to the Sale

THE LEGAL PROCESS

II. Structuring The Acquisition

- Tax & Financing Considerations Have a Significant Impact
- Never Execute a Binding Purchase Agreement Until It's Reviewed by a Tax Expert
- Alternative Structures Include:
  - Asset Sale
  - Stock Sale
  - Merger or Tax-Free Reorganization
  - Part Asset Sale – Part Contribution

THE LEGAL PROCESS

III. Negotiation & Documenting The Purchase Agreement

- Most Significant Document Which Covers the Agreement Between a Buyer & Seller
- Contains All Agreements Between the Parties Including Financial, Tax and Collateral Agreements
- Risk Allocations Are Contained in Seller Representations & Warranties

THE LEGAL PROCESS

- Seller Representations & Warranties Serve Three Buyer Purposes:
  - Useful To Obtain Disclosure
  - May Permit a Buyer to "Back Out of the Deal"
  - May Permit Buyer to Obtain Damages After Closing
- Amount of Risk is Based on Purchase Price
- Seller Goals
  - Reduce Risk
  - Reduce the Time Period for Risk

THE LEGAL PROCESS

IV. Buyer's Due Diligence

- General Information
- Financial & Tax Matters
- Review of Seller
- Employment Matters
- Real & Personal Property
- Material Documents
- Inventory
- Legal Claims

THE LEGAL PROCESS

V. Closing

- Culmination of the Entire Process
- Involves the Signing of Most Documents
- Exchange of the Purchase Price
- Has Become “Virtual” & “Cashless” in Many Cases

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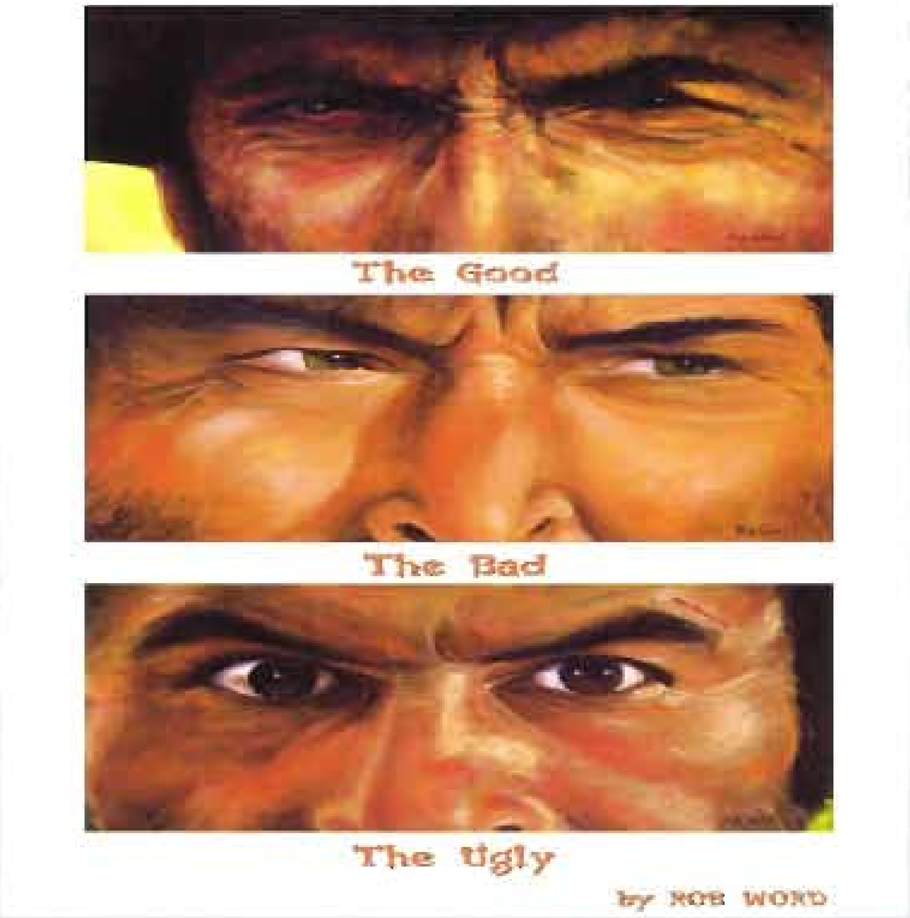
THE MARKETPLACE



THE MARKETPLACE

Buyers

- The Iceberg Phenomenon
- What do they want?
  - Pay less than Market
    - Cash, Timing, Risk
  - Minimize Risk

THE MARKETPLACE

- Types of Buyers
  - Strategic Buyers
  - Financial Buyers

What will be Sold?

THE MARKETPLACE

HOW IS THE BUSINESS VALUED

Purchase Price

=

Cash Flow

x

The Multiple

THE MARKETPLACE

"You're the only one who doesn't hate me!"

THE TRANSACTION

Two Critical Documents

- Letter of Intent
  - Define all Material Economics
- Purchase Agreement
  - Understand Reps & Warranties
  - Define Earn Out Terms

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