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Business Advisor Quarterly

A Business Law Newsletter for Owners and Executives

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Teleconference: Successfully Handle Real Estate Closings
April 14, Online Registration

Employee Privacy Rights and Wrongs
Philadelphia: May 11, Four Seasons
Baltimore: May 23, Four Points Sheraton

Insurance Recovery Breakfast Briefing: Cyber Risk and Data Theft
May 24, Offit Kurman Offices
1801 Market Street, Suite 2300

Top Ten Ways Employers Get Sued and How to Avoid Them
Philadelphia: September 20, Four Seasons
Baltimore: September 22, Four Points Sheraton

Avoiding FLSA Problems
Philadelphia: November 15, Four Seasons
Baltimore: November 9, Four Points Sheraton

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How Saleable is Your Business?

BY: JOEL LUBER

Ready to Sell?

As an attorney whose practice includes estate and business succession planning, I often assist my clients with the sale of their closely held business. On those occasions, it also becomes my job to (i) determine whether my client is at that point in his or her business life cycle where he or she is ready to sell and (ii) whether the business is ready to be sold. Both questions cannot always be answered in the affirmative.

James Laab, author of *The Business Sale System: Insider Secrets to Selling Any Small Business*, has a 10 question quiz that can provide a very good indication as to whether you and your business are ready to sell.

With scores from 0 to 5 (0 = strongly disagree; 5 = strongly agree); these are the statements:

1. I have a clear idea about what I want to do with my life after I sell my business
2. If the price is acceptable, I am prepared to take half in cash and the balance over a term of up to five years
3. Overall, I would say my business and I are in pretty good shape
4. I have 10 to 20 hours per week that I can dedicate to selling my business
5. There are no pending tax or legal problems
6. Without me, my business is not worth nearly as much
7. Sales or profits have been stagnant or declining recently
8. I have a specific price that I will sell for, not a penny less
9. I feel uncomfortable giving out a lot of financial details about my business
10. I'm worried about new competition or changes in laws pertaining to my business

To score, add the points on statements 1 to 5; subtract the points on statements 6 to 10. The highest possible score is 25. If your score is over 15, you're on the road to sale; 12 to 14, close to ready, with some fine tuning required; 11 or lower, not ready without significant preparation.

You may have thought the term "business life cycle" a bit odd or out of context. The truth of the matter is that every business and its owner has a natural life cycle, a journey that begins with hope and potential, is then propelled by success, is slowed by adversity and eventually comes to a conclusion. There are only two outcomes for every business: be acquired or to close the doors and liquidate. No owner wants to close the doors, but the undeniable fact is that only 20 percent of businesses on the market actually sell.

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A business owner may decide to sell because of life-changing events (death in the family, divorce of spouse or business partner, and illness); changes in the marketplace that cause a loss of revenues or profits; or a desire to pursue other business ventures. The most common reason a business owner decides to sell is he or she has lost the enthusiasm that created the initial spark and ultimately successful enterprise. The business can be as wildly successful as could have been imagined at the outset, be poised for even greater growth. But, if the owner is no longer willing to put in the 50, 60 or 70+ hour work weeks, to tolerate the myriad issues that CEOs must, or has lost the motivation to get up each morning to fight the new fight, it is time to sell.

The Long Vacation

You scored yourself on Laab's quiz on page one (or have come to the decision by way of alternative analysis), and you are ready to embark on the mission of sale. As you search for a business broker of good repute, the first question you should be asking is: "Do you really own your business?" This question has nothing to do with the stock or membership certificates that represent the ownership interests in the enterprise. Let me explain:

I represented a contractor, a very skilled craftsman, who did exceptionally fine, customized millwork. It started with the owner working out of his basement with a nice set of power tools, an idea and a whole lot of determination. Due to his hard work, the business grew over time. Eventually, the owner hired part-time assistants who became full-time employees and then an administrative person to handle all the office work. As the business began to grow, the owner moved the business out of his basement and into a more spacious commercial building. Soon, the business grew from 10, to 15, then 22 employees. To an outsider, the business looked very different from the company run out of the owner's basement. Yet, on the inside, it hadn't changed a bit. The owner was still doing all of the estimates, every job was customized, and the specific knowledge that was required resided only in the owner's head. When unforeseen circumstances required him to sell the business, he could not find an exit because he did not own a business. He only owned a job; it was a very profitable job, and one with 22 assistants. But, still, it was just a job. Buyers do not want to buy a job; they want to buy a business.

The lesson is clear. For a business to be transferable (salable), the owner's job responsibilities must also be transferable. Any business must be able to stand without the owner. Revenue must continue to flow after the owner exits the business. You wouldn't expect your business to grind to a halt if you take a vacation; a sale should be viewed as an extended vacation by the owner. Look, again, at statement 6 in the quiz. If your answer was a 5, you have a serious impediment to sale, one that will drive down the sale price seriously below what you estimate the value of your business to be using any set of applicable industry metrics.

Creating Salability

How do you avoid falling into this very common trap? The key is to make sure your role, as owner, is primarily general management, developing and implementing long-term strategies and growth objectives. You should not be immersed in day-to-day details of operations.

Those duties are best left to the employees who will probably stay with the business after new ownership comes in. A general tenet of all successful businesses is the "Rule of Two." Each job in your organization should be able to be handled by at least two people. The owner who spends time making sure that he or she is not the only employee performing critical functions can usually sell the business for a premium.

If you really "own" your business and not just a job, it is a matter of preparation and timing to create salability and extract the highest price from a willing buyer. Some of the key factors are:

Solid Statements. Formal (although not necessarily audited) financial statements must be available for at least three years; five years is better, with applicable tax returns. The financial statements will need to be "recast" to accurately reflect the owner's "perks" and other intra-family transactions so revenues and expenses can be restated to show what the firm will provide to a new owner.

Eliminate Weaknesses. Weed out obsolete and outdated inventory; eliminate a product line if underperforming or not profitable; sell assets (like real estate) that are not contributing to earning power.

Pay Day. Take a hard look at the financials and compare them to what you expect (or require) to be paid for the business. If the financials do not support your expectations, one or the other needs to be adjusted. This may take some time.

The Selling Memorandum. Prepare a "selling memorandum." This is the key document offered to carefully screened and qualified buyers. It should be prepared with the assistance of a business broker and your accountant with the owner playing a major role.

Curb Appeal. Spruce up the business – clean, paint, reorganize – anything that will make it more appealing to visitors. A neat, clean, organized place of business tells buyers the company is well run.

You have a great business in which you have invested your blood, sweat and tears, and now it's time to move on. You have carefully prepared. So, what's next? There is no decision more important in any business owner's life than the sale of his or her business. You were successful in creating the asset. You, therefore, are the most important factor in its successful sale. This transaction requires the assistance of trained, experienced professionals. They will not only market your business, they must be intimately familiar with the financial results of the business operations and know every detail of any major contract to which the business is a party.

Very simply, you need to rely on your business broker (investment banker), your accountant, and your attorneys. After careful consultation with all three, you will be able to say you really have a business that can be sold and that your expectations of the price and terms for that sale are realistic. Good luck!

Joel Luber is a Philadelphia based trust and estates attorney who concentrates his practice in sophisticated estate planning for high net worth clients, estate administration, and general corporate and income tax planning. He can be reached at jluber@offitkurman.com.

Is your building zoned for your use?

The building you are considering may physically accommodate your needs, but is it legal for such use?

BY: JOSEPH BELLER

Whether you are purchasing or renting, you must make your agreement contingent on obtaining a zoning permit.

Don't be Fooled by Appearance

The fact that the building has been used for a commercial or industrial use does not mean that you automatically are green lighted for your use. The history in the zoning archives may reveal that the previous use was non-conforming (prior to the zoning code now enforced) or byway of variance. In either event, a change of use by you could mean starting from scratch since the previous uses are lost by a change. Remember that a variance for a particular use is only for that use. You could find yourself with an underlying zoning designation that prohibits your desired use.

What to do

First, check the zoning designation for the address. Then check the code to see what is permitted. Remember, in addition to the code there are many "overlays" throughout the City. These are areas which are legislated by City Council. They often prohibit or require Zoning Board approval approved for uses which the basic code itself seems to permit. In some areas, there are overlays on overlays. For instance, in some parts of Center City, a beauty salon may be allowed, but a nail salon cannot locate on the first floor of the same building. Almost every part of the City has such overlays. Therefore, if you just check the zoning district, you may be misled.

Second, is it always a good thing to check your project with the City Planning Commission. They always know the latest in terms of zoning legislation.

Third, if you are going to change the building in any significant way, get your plan reviewed. The changes that may trigger a refusal for a permit because of the new code provisions (not enough parking, not enough open space, need for a sprinkler, or need for Zoning Board approval).

Fourth, make sure you don't need additional approvals from other agencies beside the City Planning Commission (Art Commission, Historical Commission, Water Department, or the Streets Department).

Demand a City Certification

All too often, the buyer does not get a City Certification from the seller despite the requirement that the seller should provide it. The City Certification advises you on the zoning designation and the legal use as well as any violations of the City Code. While this doesn't replace an inspection, it does alert you to the necessity for an explanation. You don't want to receive a summons for Court for the violation you inherited (many purchasers found out too late that the development they bought was zoned for single family).

Fair Warning

While this article is not the answer to the problem, it is meant to warn you about the possible pitfalls. A warning that bears repeating – make your agreement contingent on the zoning, and then investigate.

Commonly Overlooked Terms to Ask for When Renegotiating a Commercial Lease in This Climate

BY: NEIL RUBIN

While office vacancy rates remain relatively high, landlords are continuing to provide incentives to both retain existing tenants and attract new tenants to their locations. These incentives usually cover a combination of free rent and improvement allowances. Usually these items, as most business terms, are negotiated up front when a term sheet or letter of intent are being prepared.

While the monetary incentives may be the initial reason why tenants chose a particular location, there are numerous other provisions to keep in mind in terms of completing the lease process.

Tenants looking to execute new leases should be mindful of certain provisions in the lease which will benefit them long past the execution of the lease and for years down the road.

As an example, a non-disturbance clause will provide confirmation that in the event a landlord defaults under a loan obligation, the foreclosing lender will not terminate the tenant's lease. For a variety of factors, landlords have generally been reluctant to obtain NDA's from their lenders. Currently, landlords appear to be more willing to use some reasonable efforts to obtain them both from current lenders and future lenders for the benefit of the tenants.

Another area where landlords have shown willingness is the release of any lien rights to tenant's personal property in the premises. This can be critical for if a tenant defaults, as most leases provide for the landlord to have a lien against such property and the right to seize it to pay off any past due rent or other charges. Recently, we have been more successful in having landlords waive these rights which means that even if a tenant were in default, they would be able to keep and remove their property which obviously can make any set up in a new location much more efficient and not as costly.

There are *many* provisions similar to these examples where some advance planning can be well worth it when a problem may arise numerous years into a multi-year lease, which issues aren't even on the radar at the time of the lease signing.

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Tips to Successfully Gaining Concessions From Your Union Without a Strike

BY: JULIUS STEINER

One of the most difficult tasks for management to accomplish successfully without conflict often presents itself during economic recessions:

The need to go to a union and request concessions or "give backs". This usually occurs during negotiations upon contract expiration but can also take place during negotiation of an initial contract or even mid-term.

The traditional approach usually involves a request for re-negotiation of wages. This is generally countered by a strike threat. It is clear that this tactic will provoke a confrontation which can lead to extended, negative, and unpredictable results. I have found in over 30 years of experience that utilizing a more thoughtful and strategic approach yields results that are less negative and destructive.

How do you do this?

1. First, management must clearly know what it wants and why
2. Management must be able to articulate this need in very clear and basic language -- it is important to define the problem
3. Be able to demonstrate how the requested concession will actually solve the problem
4. Be able to support your position with facts and figures -- provide the union (i.e. its auditor) with complete access to all relevant information; transparency is crucial
5. Be prepared to answer the inquiry "…if we give up what you request, when will we get it back?"
6. Be prepared to answer the last question in the equation – "What else will you give us?" This may take the form of some sort of enhanced job security during the term of concessions or something new like implementation of "Gain Sharing"

Julius M. Steiner is a well known Philadelphia labor and employment attorney with a unique blend of over 30 years experience as a practicing attorney and CEO. He can be reached at jsteiner@offitkurman.com.

About Offit Kurman

Offit Kurman is a dynamic full-service law firm assisting clients in the mid-Atlantic region. Our team of Philadelphia attorneys are legal advocates who are experts in all aspects of commercial litigation, business law, real estate, estate planning, health care, labor and employment, construction law, government contracting, estate and trust administration, asset protection, and insurance recovery. For more information about Offit Kurman, please visit us on the web at **www.offitkurman.com.**

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