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Exit ahead:

The ultimate guide for business owners preparing for succession or sale

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Contents

Introduction

Selling or transitioning out of a business that you've created, or bought and built, over many years can be a stomach-wrenching exercise. There's a lot to think about, people to consider, a myriad of critical decisions to make, and actions to take to achieve the best succession or sale outcome.

One of the many positives about being a business owner is that you don't have to traverse this critical juncture alone.

This report charts a road map for small and medium-sized (SME) business owners to help them prepare for and successfully transition out of their businesses – whether it be in full, or part, to family members or an external third party. Creating a business that survives its initial years and grows into a sustainable and thriving enterprise is not a given.

Just **77% of new business entrants** survive their first year

only **51% are still operating after three years**[1]

Therefore, it's critical that business owners make the same time, financial and emotional commitment to the succession or sale of their business, as they've poured into starting, growing and running it.

[1] Counts of Australian Businesses, including Entries and Exits, July 2019 – June 2023 | Australian Bureau of Statistics (abs.gov.au)

Business succession or sale on your mind?

Australia has a dynamic business landscape comprising more than 2.5 million businesses operating at every stage of the business lifecycle – start-up, scale-up and maturity. Divesting your financial and or operational interests in a business requires careful consideration, planning and execution. Every journey will be different, with the strategy specifically tailored to the objective of the business owner, the value and size of the business, and the sector in which it operates.

Reasons for sale

There are a range of reasons why businesses change hands. Most often the circumstances are planned, such as the owner retiring and wanting to realise wealth tied up in the business, or they want to grow the business's competitive advantage, with the help of a strategic acquirer, so they can step back from the day-to-day running. However, sometimes unforeseen circumstances force succession or sale, such as an owner's ill-health, surprise interest from a competitor or other buyer, as well as favourable or unfavourable market conditions.

Planning ahead is critical

Business succession can be complex and risky, particularly if it's done too quickly, and without proper planning, adequate due diligence, and a clear strategy. It can also be disruptive for employees, suppliers, and customers.

Best practice would see business owners working on a succession or sale strategy well before they intend to pass on or sell the business. This plan should include a range of possible options and be regularly revisited and refined every year as the business grows and matures. It should also take into account market forces at play including changing business conditions so that it can be enacted quickly if circumstances demand it.

This plan should align closely with your strategic business goals. These goals broadly fall into the following categories:

- **Creating a disruptive business or technology that may change ownership quickly**– this may have involved attracting start-up venture capital.
- **Building and expanding a medium-term business** – this may have involved attracting critical skillsets, injecting additional capital through debt finance, debt funding, investors or injecting your own personal capital.
- **Maintaining and sustaining a long-term business, such as a family business** – this may have involved several stages of workforce expansion, capital raising, purchases and restructuring.

Business Insight

A proven business model that delivers sustainable growth over time is a key selling point. **In 2022-23, the number of businesses that recorded revenue of $10 million or more increased by 12%.** This was primarily driven by about 7,000 businesses experiencing growth that shifted them out of the $5 million to less than $10 million revenue category and into the $10 million-plus club[2].

[2] Counts of Australian Businesses, including Entries and Exits, July 2019 - June 2023 | Australian Bureau of Statistics (abs.gov.au)

Have the confidence to balance risk and reward.

The 3Ps of a successful succession or exit strategy

Achieving the best succession or exit outcome relies on having a well-planned, deliberate and timely succession or sales strategy. This means getting a fair price for your business, negotiating reasonable exit terms and after-tax results to ensure you have the best retirement options, and a smooth handover to the new owners.

The 3Ps of a successful succession or exit strategy are:

- **Purpose**
  What do you want to achieve? Full sale or partial sell-down and to who – family, investors, shareholders, a competitor, or employees?
- **Preparation**
  Who would be interested in your business? How would you find them? What makes your business attractive to them and therefore maximises your business value?
- **Process**
  Which exit option is the most appropriate to help you achieve your goals and deliver the best outcome?

Business decisions are never made in a vacuum. External factors, such as the state of the economy, industry, market and regulatory environment in which your business operates, as well as global geo-political events, can influence the value of your business, market or investor demand, and timing of sale.

Keeping an eye on economic forecasts, particularly related to the cash rate and inflation, can help business owners and their advisors plot a succession or sale strategy that is timed to take advantage of strong economic conditions. On the buy side, buyers and investors will also use these forecasts to inform their decisions about capital avialability and the price at which they will transact.

Is it the right time to exit? The economics of good timing

The Reserve Bank of Australia's (RBA's) forecasts on inflation, monetary policy, unemployment, and wages hold significant implications for businesses and their operating environment. Monitoring RBA forecasts, in particular, can not only help business owners adapt their strategies and manage costs, but they can also inform the design and timing of a business sale to take advantage of strong market conditions or to get in ahead of a potential economic slowdown.

Key economic indicators

Economic indicator	Status	What it means for businesses now	Forecast for June 2025
Cash Rate	4.35% February 2024	Cost of capital, borrowing and debt servicing costs remain elevated	3.6%
Consumer Price Index (CPI)	4.1% Year ending December 2023	Household, material, and supply costs are moderating but remain elevated	3.1%
Unemployment rate	4.1% January 2024	Availability of labour remains tight but is improving which is putting some downward pressure on wages. However, there is a mismatch between demand and supply of some skillsets	4.4%
Wage Price Index	4.2% Year ending December 2023	The cost of labour remains high, but is expected to moderate	3.6%

Source: Australian Bureau of Statistics (ABS), 2024 and the Reserve Bank of Australia (RBA) 2024[3]

[3] In Brief: Statement on Monetary Policy – February 2024 | RBA

Step 1:

What do you want to achieve? Be clear about your **purpose.**

Every business owner's sale or succession plan will be different and will be shaped around the individual circumstances and characteristics of their business and most importantly, the objective they want to achieve.

This could be to:

- optimise retirement options and divest fully
- transition management and or ownership to the next generation
- find a business partner or investor to purchase a percentage of equity in the business
- grow the business and take it to the next level with a private equity partner or by listing it on the Australian Securities Exchange (ASX), while potentially remaining a shareholder

In some circumstances current business owners may be required to remain working in or alongside the new owners for a period to ensure a successful transition. This is usually negotiable as part of the sale or succession process.

Is Australia on the cusp of "the greatest business ownership transfer" in history?

The largest transfer of intergenerational wealth in Australia's history – $3.5 trillion – is forecast to occur by 2050[4].

At the same time, Australia could also face a seismic shift in the business landscape –"the great business ownership transfer." The captains of Australian small businesses are ageing. About 50 % are over 50, with 22 % over 60 and nudging retirement, according to the Australian Small Business and Family Enterprise Ombudsman analysis of Census data[5].

In 2021, the most common age of a small business owner in Australia was 50 – five years older than they were in 2006. This is in stark contrast to the 1980s when there were twice as many owners aged between 30 and 49 as there were aged over 50.

It's not a trend that's being mirrored in other Asia Pacific countries, with Australia having the highest proportion of small business owners aged 50 years and older, according to CPA Australia's latest Asia-Pacific Small Business Survey[6].

Potential reasons could include market volatility – business owners have assessed that they'll make more money staying in the business than selling it and investing the proceeds in the share market. No identified successor could also be keeping older owners at the helm for longer.

4 Wealth transfers and their economic effects - Commission Research Paper - Productivity Commission (pc.gov.au)

5 Small Business Matters | ASBFEO

6 Asia-Pacific small business survey | CPA Australia

Step 2:

Are you ready? **Preparation** maximises value.

Initial questions to ask

Once you've established a clear objective and purpose for transitioning out of your business, it's important to consider the following matters before you commence what will be a detailed and lengthy preparation process.

Who would my business be attractive to?

Assess who would be interested in your business and put together a list of potential buyers or investors. These could be:

- family members
- management within your business
- competitors, customers or suppliers, both domestically and globally
- private equity

What am I selling or transitioning?

Be clear about exactly what you want to sell. For example, are you selling the business in its entirety or a part of it? Are you selling assets or the issued shares?

Also consider what will be included and excluded, particularly in the case of family businesses where personal assets may be tied up in the business.

Do I want a public or private sale process?

Determine early if there are any family or commercial reasons why you would not undertake a competitive bidding sale process. Competition is central to achieving value, particularly in a trade sale. However, some business owners may wish to keep employee details and commercially sensitive information, such as customer lists, private. This may require a more bespoke bilateral sale process with one or two prospective buyers.

Preparation prior to sale is crucial

Preparation means getting your business into a position where it is effectively "investor-ready" or "sale fit" well ahead of the time you plan to hand over the baton to another family member or to take it to market. Preparation also minimises the risk of potential surprises arising when prospective purchasers or investors are undertaking a deep dive into your business during the due diligence period – surprises that could compromise a transaction or make parties walk away.

What makes a business attractive to an investor?

- **market size**
  - scale and or sustainable growth
- **structurally attractive industry**
  - strong gross profit margins
  - quality customers with strong credit features
  - recurring, repeatable, or contracted revenues
  - barriers to other businesses to enter
- track record of sustained profits, growth and a competitive advantage
- experienced management team
- strong business systems and technology
- high conversion of accounting profits to free cashflow

Transitioning out of your business is not an overnight process. A well-conceived and executed succession or sale plan, whether it's by a trade sale, management buyout or Initial Public Offering (IPO), is a multi-year process.

Planning and preparation will put your business in the best shape to transition to other family members or to attract the right buyer or investor, using the right succession or sales strategy, at the right time, to maximise value.

The final countdown (to succession)

5 years from lift-off

- Write down your succession objectives
- Consider what the external market is currently doing and how it will perform in five years
- Consult spouse and stakeholders

3 years from lift-off

- Establish a management team with the capability to drive the business forward
- Begin to transition key roles and relationships
- Document systems and processes
- Consider incentive structures to retain key management

Key factors in the timing of sale include:

- Economic cycles impacting the business
- Timing of major customer contract renewals
- Key business milestones
- Lease renewal dates
- Tax considerations, eg CGT concessions
- Stage of business growth cycle

2 years from lift-off

- Establish and deliver on a business plan focused on sustainable growth
- Identifying negative value drivers and take action to address or mitigate them
- Secure customer relationships through contracts
- Ensure robustness of financial information – audited financial statements and reliable management accounts will provide buyers with greater confidence
- Adopt consistent accounting practices in accordance with Australian Accounting Standards
- Review stock levels – many private businesses hold excess stock, which should be monetised ahead of the business sale
- Ensure related party arrangements are on arm's length terms

1 year from lift-off

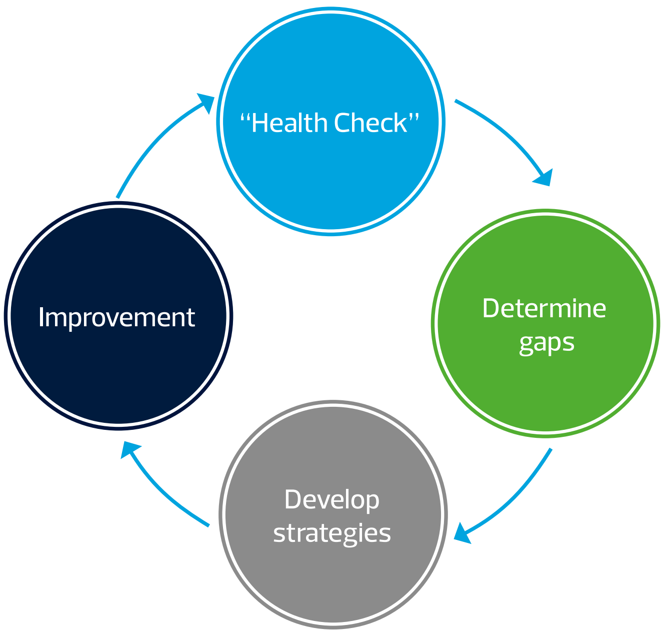
- Many private businesses are highly reliant on the business owner and may also employ other family members
- Buyers will be concerned if much of the goodwill resides with the business owner, rather than the business itself – eg key customer and/or supplier relationships

If the vendor plans to leave the business, it will be important to:

- Establish a broader management team with the capability to drive the business forward
- Transition key roles and relationships
- Document systems and processes
- Consider the ongoing role of family members
- Consider incentive structures to retain key management

Pre-sale business health check

Every business owner should undertake a health check on their business ahead of preparing for sale or succession. This is often called "exit readiness" or "vendor due diligence" and enables business owners, with the support of their advisors, to run a fine-tooth comb over their business to identify risks, issues and gaps, and to implement measures that will improve the value of the business before going to market.



Take RSM's Business Exit Readiness Survey to see how well prepared you are for succession or sale.

Our view – the Top 10 requirements (the 'givens') when preparing for sale

1. People	☐
2. Products and service (market)	☐
3. Sustained profitability	☐
4. Customer list	☐
5. Financial reporting	☐
6. Relationships transitioned	☐
7. Systems and internal controls	☐
8. Information technology	☐
9. Corporate governance	☐
10. Legal and contractual	☐

Business preparation checklist

Potential purchasers or investors will want to assure themselves that your business has a proven business model, clear growth strategy and strong fundamentals underpinned by robust and standardised systems and processes.

This checklist is not an exhaustive list of issues to consider, but should serve as a provocation to owners about the breadth and depth of information required as part of the sale due diligence process.

1. People

Profits and business performance are not reliant on one key personnel member, such as the owner.

Preparation:

- put in place a management team, if not already in place, with key performance indicators and formal performance appraisals
- ensure compliant employment agreements are in place, and assess whether incentive schemes or employee share options are required or beneficial to motivate and lock-in key staff and skillsets
- ensure compliance with workplace health and safety requirements
- assign customer and supplier relationships to management and ensure contracts are in place, particularly with key customers or suppliers

2. Products and service

Robust business and market data shows continued demand for products and services.

Preparation:

- identify and explain your competitive market advantage
- have critical business data, such as market share, readily available
- demonstrate future growth or demand
- ensure intellectual property projections are in place for trademarks, patents or copyrights

3. Profitability

The size of the market is large enough to sustain the business and provide growth opportunities.

Preparation:

- understand the addressable market and its dynamics and growth prospects
- focus on margin preservation and growth, and understand the levers for margin expansion
- assess business labour capacity and ability to achieve productivity improvements or expand the business
- assess risks for market or industry disruption and develop mitigation strategies across areas such as labour and pivotal suppliers

4. Customers

Diverse and contracted customer base.

Preparation:

- assess your customer spread to ensure your business is not reliant on a few customers or clients, or is concentrated in one or two industry sectors
- review customer contracts and rates to ensure they are market-appropriate
- demonstrate customer profitability

5. Financial reporting

Informative, timely and accurate reporting.

Preparation:

- test your systems to ensure they can produce meaningful monthly reports on key financial metrics such as profit and loss and cashflow
- ensure projections and forecasts are underpinned by robust and detailed assumptions
- consider non-financial reporting such as Environment, Social and Governance (ESG), including climate risk, and other reporting to demonstrate business performance and success

6. System and internal controls

Business processes and procedures are well documented, understood and up to date.

Preparation:

- record or update business procedures and processes
- business records are well organised, current, and backed up
- security and privacy measures are in place to protect business data

7. Information technology

Technology is up to date, fit-for-purpose and secure.

Preparation:

- update outdated hardware or have a plan to transition to the cloud, if appropriate
- software licensing agreements are in place and current
- recovery plan is in place and is regularly tested
- business data is accessible from remote locations
- the business has a digital strategy, including for the digitisation of any manual business processes

8. Corporate governance

Appropriate governance structures are in place.

Preparation:

- put in place or review existing shareholder's agreements to ensure they align with business objectives
- company records and register are up to date
- simplify corporate and tax structures if required, particularly if only part of the business is being sold
- ensure all legal, legislative, regulatory, and professional standards are being met
- consider if it's time to set up a Board of Directors with suitably skilled external parties

What's your business worth and what will a buyer pay? Valuation vs price

The desired outcome of any succession or exit strategy is to achieve a fair and satisfactory transaction. Completing the transaction comes down to finding a balanced compromise between what an owner believes their business is worth, and what a purchaser is willing to pay, to own or invest in it.

Business owners can inform their expectations and a defensible price position by undertaking a valuation of their business.

Valuation is a formal quantitative process to derive a business valuation that includes capitalisation of earnings and discounted cashflow methods.

Purchasers may not always agree with the valuation or the key assumptions behind it, and will put forward a price at a point where they see value. This can then become a negotiating point. Sometimes buyers will pay more if they see the strategic value or synergy that can be achieved by an acquisition.

Price is the agreed point between a seller and buyer that a business can transact at and could be impacted by factors such as industry consolidation, level of capital availability in the economy and the strategic attractiveness of the business.

Step 3:

How do you pass on the business baton? The exit **process.**

The sophistication of private and public capital markets and the proliferation of new private investment funds and vehicles, including the rise of the family office in Australia, has created more opportunities for business owners to attract investors to help them transition out of their business, in full or part.

***Your succession or sale options will primarily be influenced by the enterprise value of your business.** This enterprise value may also be impacted on by a range of qualitative factors specific to your individual business and market demand*

Below are **seven key succession, sale and exit options:**

- Family succession
- Management buyout
- Trade sale
- Private equity
- Family office
- Initial Public Offering (IPO)
- Orderly wind down

Business succession, sale and exit options by business value

Enterprise value	Succession, sale and exit options
Less than $10 million	Family succession management buy out trade sale orderly wind down
$10 million – to less than $20 million	Family succession management buy out trade sale SME-focused investment vehicles/funds family office
$20 million - $200 million	Family succession trade sale family office private equity
More than $200 million	Family succession trade sale private equity IPO

A new SME-focused investor

Have you heard of the Australian Business Growth Fund (ABGF)? Established in late 2020, the fund was set up with $540 million seed capital from the Australian Government and a group of major lenders to help SMEs access equity finance to support their recovery from the economic disruptions of COVID-19.

According to ABGF, its mission is to **"help Australian SMEs realise their growth ambitions without business owners having to relinquish control"**[7] .

The fund invests between $5 million and $15 million into eligible businesses in the form of:

- ordinary shares, preference shares, loan notes and convertible notes, or a combination
- optional release of cash out equity to owners/founders
- minority investments of up to 49%

Eligible SMEs need to fulfil the following criteria:

- Australian headquarters
- turnover of between $2 million and $100 million
- three years of profitable operations
- clear growth strategy

Snapshot of succession and sale options

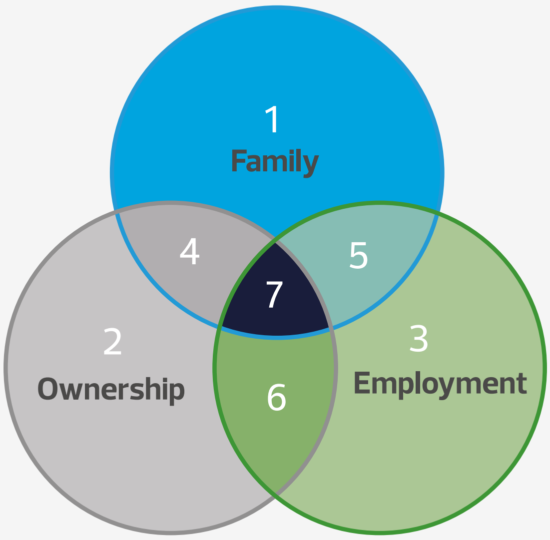
Some business owners, particularly those at the helm of larger companies, may consider pursuing one or more sale options, such as a trade sale and IPO, to give them flexibility to choose the one that promises the best outcome. All options have different legal and tax implications that need to be considered and managed, including having suitable arrangements and agreements in place with customers, suppliers and employees who are critical to business continuity.

Family succession

Keeping a business in the family is becoming increasingly difficult as younger generations forge their own career paths. That's why succession planning – identifying who is willing and qualified to lead the family business – is more important than ever, particularly as older business owners approach retirement.

Key considerations:

- map the employee, director, and ownership relationships to understand the level of involvement and investment of all family members – there are many variations that can impact succession planning dynamics
- align family and business goals such as through a family charter
- maintain transparent communication between all family members
- engage a third-party intermediary to undertake negotiations between family members



Move from 1st to subsequent generation

[7] Home - ABGF

- update or put in place shareholder agreements that include buy-sell agreements
- what form will the ownership transfer take?
- how will it be funded?
- obtain concurrent estate planning advice

Management buyout

Typically, a management buyout involves existing members of a company's management team or
an external team putting forward an offer to buy out all, or part, of the company from the current owner. Usually, this involves debt funding or co-investment with a private equity firm. It can be a smoother transfer because of the continuing management team's knowledge of the business and its operations. It can also form part of a succession planning strategy in a family business.

Key considerations:

- obtain advice regarding managing conflicts of interest and access to commercially sensitive information from the management buy-side during the process
- buying out current company shareholders
- bringing in an independent advisor to evaluate the proposed agreement
- ability of management to obtain financing
- alignment of management team's values with the owners' mission, vision and values

Private equity

Private middle-market companies continue to be key targets for private equity firms. These firms look for businesses with strong fundamentals and a track record of performance but are in need of capital and expertise to grow and expand.

Private equity firms acquire businesses using capital from investment funds they operate on behalf of institutional investors. They can buy a majority or minority stake in a business, depending on its particular circumstances.
In family businesses, private equity can help foster the skills of second or third generation family members to step into management roles.

Key considerations:

- the private equity investment horizon is generally short to medium term with firms most likely to seek a liquidity event within three to five years, however some firms may put in place longer-term arrangements, depending on the industry sector
- alignment of the owner's business mission, vision and values with that of the private equity firm
- industry-specific or technical knowledge of the private equity firm

Private equity firms may take different deal approaches depending on the industry sector. For example, firms may inject long-term capital into an agribusiness, in the form of a land purchase, while entering a joint venture with the farm owners to operate the business. RSM explored the potential sources of funding available to agribusinesses in this report .

https://www.rsm.global/australia/report/strategies-securing-funding-australian-agribusinesses

The rise of the family office

Family offices are private advisory and investment firms set up by high-net worth families primarily to manage their wealth and investments. Some make strategic investments in small to medium-sized businesses, that are attractive and whose values or operations align with their family legacy. The number of family offices operating in Australia has grown over the past decade.

Trade sale

A trade sale is a transaction involving the sale of one business to another, such as a smaller business to a competitor or larger company, often in the same industry sector. It can be a merger or an acquisition.

Key considerations:

- have a clear strategy
- choose a marketing option that takes into account any commercial sensitives:
  - broad auction
  - limited auction
  - targeted auction
  - exclusive negotiation
- is it an asset sale or a share sale?
- if a competitor is the purchaser, will the deal require Australian Consumer and Competition Commission (ACCC) clearance?
- continue to drive business performance during the sale

Initial Public Offering (IPO)

Taking your business public is a major step that requires significant planning and can take from six months to two years to complete, depending on the complexity and size of the business and the sector in which it operates. Businesses need to meet minimum requirements under one of two tests - a profits or assets test – to list on the ASX.

Key considerations:

- businesses are subject to a higher level of public scrutiny
- increased level of reporting requirements, including continuous disclosure protocols, and increased regulation
- pre- and post-listing costs such as the preparation of expressions of interest, disclosure and contract documentation and the establishment of a Board comprising Directors with ASX-listed experience
- increased cost and administrative requirements, such as appointing a company secretary
- loss of competitive market advantage as a publicly traded company

Dramatic drop in listings on the ASX

There has been a significant drop in companies listing on the ASX. In 2023, just 37 companies listed. This was 56 fewer than the 93 that listed in 2022 and 158 fewer than the 195 companies that went public in 2021[8].

Orderly wind down

This is an incredibly difficult decision for any owner to make. But if a frank assessment of the business's revenue and profit, customer base, market position, and prospects for growth determines the business does not have the required profile for sale, and there are no family members to take it over, winding it down may be the best option.

For businesses that have assets, such as equipment or property, this can be sold and the value realised quickly. If the business has stock or inventory to sell, this can be done over a period of time, such as via an extended "closing down sale", to recover working capital out of the business before ceasing trading.

Top reasons why a business sale fails

- external forces such as COVID
- lack of planning
- excess business complexity, such as its structure
- people with a stake in the business (not bound by a buy-sell agreement) not signing off
- due diligence turning up issues
- Board of the prospective buyer not approving the purchase

[8] Company directory (asx.com.au)

Drive new growth by expanding across borders

Assembling your business succession team

Whatever succession or sales strategy you choose, business owners will need a multi-disciplinary team of professionals to manage and undertake the process, led and coordinated by a project leader. The skillset mix of your team will be determined by the succession or sales strategy you choose and often your industry.

We've identified key advisors and the type of expertise they can provide to support a business succession or sale.

Mergers and Acquisitions (M&A) Advisor

- act as an overall project manager
- preliminary business valuation and gap analysis
- help business owners:
  - for sale by preparing relevant sale documents (such as information memorandums and process letters) and identifying possible buyers
  - market the business and assess offers
  - negotiate a transaction and get to financial close

Accountants

- preparation of financial statements
- vendor due diligence services
- tax planning and structuring to extract a higher after-tax sale consideration for the owners
- working capital calculations
- estate planning – particularly for family businesses
- capital gains tax implications – applicable concessions and liabilities
- transfer duty and land transfer
- allocation of purchase price

Lawyers

- legal due diligence
- contractual agreements
- regulatory approvals

Other Advisers

- real estate agent if the business includes property
- insurance
- industry-specific consultants to support the IPO process

How RSM can help

RSM is the sixth largest network of assurance, tax and consulting firms in the world, with 32 offices and more than 1,800 staff in Australia alone.

We work closely with thousands of small to medium enterprises across the country, in sectors ranging from agribusiness to technology (and everything in between).

Our people pride themselves on building a high level of expertise within their chosen sector, so they can speak their clients' language and offer true value to support their business.

To find out how our experienced business advisors, corporate finance experts and financial planners can work with you to **prepare for and stage a family succession or execute a full or partial sale of your business**, please contact your local RSM office

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