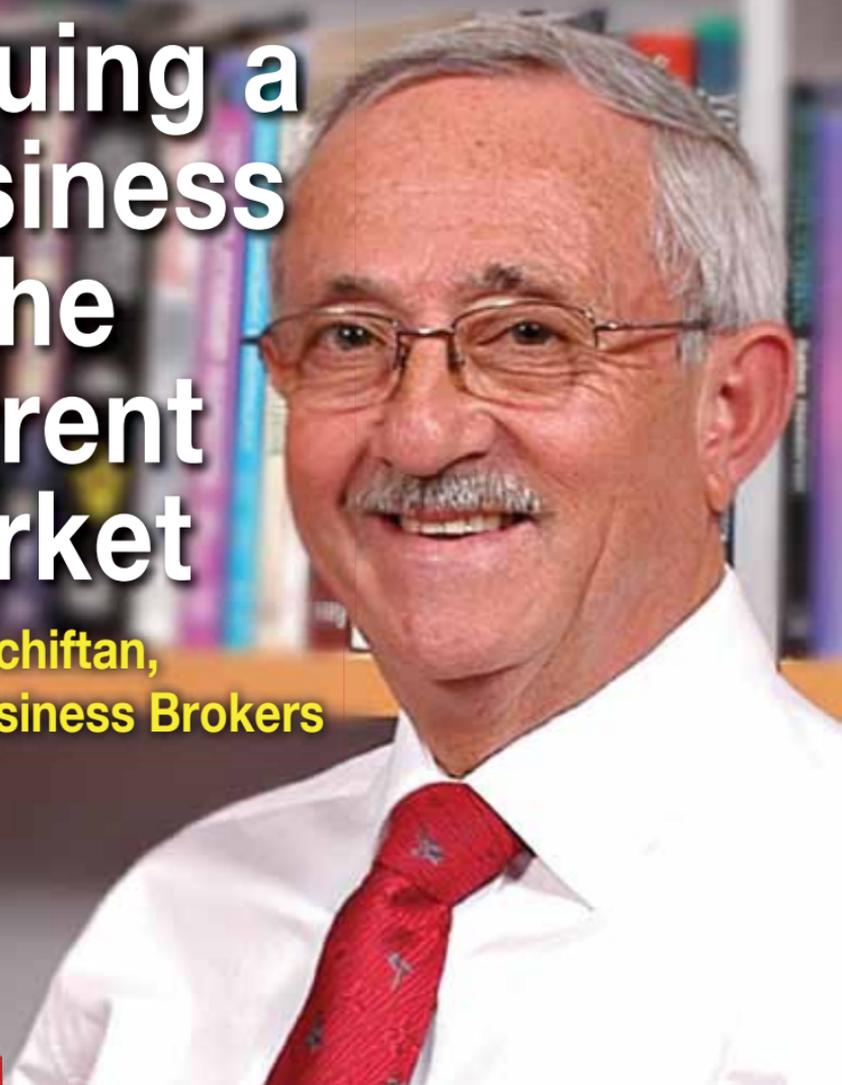


# Valuing a business in the current market

Peter Schifftan,  
P+S Business Brokers



Chartered Accountants Business in Focus

Monthly audio program

April, 2011

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The divorce rate's up, families are becoming ever more complicated in their blended relationships, and many Australians now are from overseas. What does this mean? Complex issues for estate planning. In this edition, we investigate the intricacies of comprehensive estate planning these days and what it takes to ensure the safety of your clients' financial futures. We also discuss estate planning in the area of self managed super funds. It's an important and growing area for accountants as increasing numbers of people go the do-it-yourself super way.

Your client's thinking of selling up, but what's the business worth? Veteran business broker Peter Schifitan offers his experienced views, with an update on what's really happening in the business buying and selling market right now. And, as business operators start thinking about budgets for the financial year ahead, we take a timely look at salary benchmarking and packaging.

Tax expert Michael Jones returns to the topic of excess super contributions this month with a ten-point action plan to help your clients stay out of trouble with the Tax Office, while Ron Baker of VeraSage Institute in the US returns also, with more reasons and ways to ditch the billable hour and start pricing on value instead.

And we can't ignore the major global events dominating our headlines in the past month, including conflict in North Africa and the Middle East and, of course, the catastrophic events in Japan. We assess the impacts on our own economy and sharemarket.

Plenty of great advice this month – I trust you'll gain value from it,

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Merv Lobb will be presenting on this topic at the Institute's Winter Tax School and Tax & Super Forum in April and May. For details, please contact the Institute on 1300 137 322

### **VALUE PRICING & THE DEMISE OF THE BILLABLE HOUR**

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# **THE ESSENTIALS**

## **April 2011**

### **Track 2**

#### **Valuing A Business In The Current Market** **Peter Schiftan, P+S Business Brokers**

- It will be a very difficult 12 months, particularly for selling small businesses. Those with \$1 million-plus revenue and good, sustained profits will be sellable, but securing funding is still tricky
- The more profitable businesses at present are in the service sectors: larger trading groups, recruitment, traffic management, rent rolls, IT companies, wholesale import and export companies
- Manufacturing, engineering and retail are down to very low multiples, though some chain retailers are attracting attention from overseas
- Selling restaurants is nearly impossible - there are just too many
- Mergers are becoming more common - we've never been busier with buyer advocacy work, finding businesses that others can bolt on to their existing operations
- Both buyers and sellers today are very smart. Many buyers already have an exit strategy in

mind, maybe only 3 to 5 years away. They're looking for businesses with sustained profits

- There are many ways of valuing a business. I look first at EBIT - earnings before interest and tax, then whether the sector is in demand
- What buyers want is a return on investment. If they can't see 25 to 30 percent after everything's taken into account, they'll walk away
- I want to see figures from at least 3 years, audited if possible, plus management accounts for the current financial year
- I advise would-be sellers not to take their eye off the ball in running the business. It's not sold until the money's in the bank
- Once brokers have valued a business and decided to list it, they will work closely with the vendor to prepare for due diligence and assemble the paperwork
- They also have a duty of care to the buyer to ensure that everything is in order
- Goodwill and brand can add value if a buyer can see that the business has a distinctive place in the market, and sustained profitability, but it's subjective
- The most common mistake people make is deciding to sell too early or too late. When the business is rising, with plenty of potential, that's the time to sell, not when it's plateaued
- And be prepared: don't have cash, have your financials in order, proper stock figures, clear contracts and agreements, so that a broker can tell a good story about your business

## Track 3

### Economic Update

Professor Neville Norman, Melbourne University

- Just after Christchurch, the Japanese earthquake and tsunami. Immediate effects on stock prices, and both immediate and enduring effects on insurance costs. Reinsurance has now reached its limit; premiums will rise
- For businesses in Australia, other effects will probably not be serious or longlasting. Indeed, there may be positive outcomes for some risk consultants, energy consultants and construction firms
- But the international events will add another pro-inflationary factor to energy prices, as will the Federal Government's decision to re-introduce its carbon pricing/carbon tax strategy
- I believe no such tax will get anywhere without bipartisan support, of the kind afforded the North-west Cape Gas Shelf project 20 years ago
- It's cheap politics for the opposition to condemn it, and for the government to make a short-term arrangement with the Greens to push it through
- On the forthcoming Federal Budget, it will be important to look at timing - when the government projects it will receive revenue from things like the carbon tax
- And when will the government expect to be back in budget balance - likely to be longer now than I've previously forecast, because of international events and some domestic ones
- The government needs more money, so watch out for tax changes - some trimming of the

stimulus packages still in effect, and there's a Treasury push to increase excise on things like tobacco and alcohol

- On interest rates, I still think there'll be one more increase before a decline later in the year
- That means for business, if you're entering a new loan, the case for fixing rates is not that strong. Nor is the case for changing an existing loan to a variable rate
- The Australian economy is growing moderately - not fast enough for me, but fast enough to avoid any risk of a double-dip recession
- But too many people are gloating that Australia's was the only developed economy to avoid recession. In fact, most others are now growing faster than we are. We mustn't be complacent

## **Track 4**

### **Estate Planning In A Socially Complex World**

**Louise Bedson, Tresscox Lawyers**

- In preparing a comprehensive estate plan, we need to consider the goals of the client, how they want their business to look in the future, who's going to look after their assets in the case of loss of capacity, who the client wants to benefit from the estate and who needs to be protected
- The likely risks to the estate also need to be taken into account, e.g. divorce or bankruptcy
- The estate plan should go hand-in-hand with succession planning for the business and should be reviewed every 3 to 5 years, or as circumstances change

- Our social landscape has changed: we're wealthier, we live longer, divorce rates are up, blended families more common and many more of us have overseas family connections
- So we need to understand the client and his family, and how ownership of the assets in the estate is structured
- Family law issues may arise where second or later marriages are concerned, or where adult children are entering into other relationships
- The possibility of claims from disgruntled beneficiaries under the Succession Act can also be reduced through careful estate planning
- It may also be necessary to make provision for vulnerable beneficiaries through, for example, a testamentary trust
- International considerations are arising more frequently, with people living or working overseas and subject to other jurisdictions, which may have different laws
- Superannuation also needs to be considered. It doesn't automatically form part of the estate, but - with so many people having self-managed super funds - has to be carefully thought about in terms of the wishes of the individual client
- Potential loss of capacity must also be taken into account. Who will run the business? How will the client be cared for in that event?
- A detailed check list, starting with the client profile, will be worked through to ensure that the client's wishes and every possible eventuality can be considered and dealt with

## Track 5

# Current Issues Facing SMSF Accountants

## Merv Lobb, Simple Super Solutions

- The self-managed super fund sector is the fastest growing superannuation sector in Australia
- And we're all growing older so this is an important and growing area for accountants as they manage their clients' superannuation affairs - they need to get their minds around what the real problems are
- Estate planning is important to make sure that the deceased person's wishes are complied with
- This means putting systems and processes in place to make sure the member's wishes are adhered to regarding, for example, who will receive the superannuation death benefit, what form will it be paid (a pension or lump sum) and what will be the tax consequences of how it's paid out
- Recipients will either be dependants (tax free) and non-dependants (adult children no longer financial supported)
- It's important that the trustee can't use his or her discretion regarding the proceeds of the fund but that the member's wishes are followed
- There are binding death benefit nominations which are becoming very popular now. This allows the member to give thorough instructions to trustees about where the proceeds should go - a document enforceable by law
- A will on its own is useless when looking at the disposal of superannuation assets

- Excess Contributions Tax has become quite an issue now. The tax office is focussing in on this now so it's important that everyone keeps an eye on how much they are contributing into super
- This falls into 2 areas: concessional and non-concessional:
- Concessional is the amount you can pay into your super fund as a deductible expense
- Non-concessional is money going into super that we've already paid tax on. It will not be taxed again either going into the fund or being withdrawn from the fund, as long as the annual limit of \$150,000 (or \$450,000 over 3 years) is adhered to. This is the area that the Tax Office is watching.
- A major compliance issue with the ATO is to encourage trustees to lodge self-managed super funds returns on time. Self-managed super funds that don't lodge on time run the risk of being made non-compliant by the ATO and this has serious tax consequences.

## **Track 6**

### **Value Pricing And The Demise Of The Billable Hour**

**Ron Baker, VeraSage Institute, USA**

- Professional firms continue to charge by the billable hour because that's what's they're used to. But that doesn't make this age-old system good. You won't optimise your offering to clients by continuing to do what's always been done

- I wrote my new book to share all the wisdom we've accumulated over the past few years, and create a one-stop book about implementing value pricing and a new business model for the professional firms of the future
- There are 3 main themes in my book: 1) We have to change the predominant business model from selling time to selling intellectual capital, in the process transforming a professional services firm to a professional knowledge firm. 2) We provide strategies to help firms create more value. If you can create more value for the customer, then you'll capture more value for your own professional firm. 3) We offer an 8-step process for implementing value prices
- The difference between Value Billing and Value Pricing: billing takes place in arrears, pricing's done upfront. Customers want certainty in pricing and that's what is being offered with this radical approach, it's much more appealing to customers

## **Track 7**

### **Salary Benchmarking And Packaging**

**Laura Birley, People Dynamics**

- To make sure you're paying the right salary levels, you need to do an internal and external comparisons
- Have a look at salary benchmarking tools such as you'll find from Seek, CareerOne, MyCareer, or the Australian Institute of Management AIM
- People will talk about how much money they're getting so beware paying different amounts to

staff doing the same job - there will be perceived inequities

- You mustn't ignore those who don't ask for a pay rise - often they're your best employees
- Salary packaging is often used to attract staff - it's an arrangement whereby you can help employees "buy" with their pre-tax income, reducing their tax liability. Makes sure you get the right advice from your professional adviser or accountant
- The ATO provides a list of approved items, such as novated leases, superannuation or childcare
- You need to be aware of Fringe Benefits Tax
- If you have agreed with staff members that you'll review their salaries every year, then it's important to do so or you could be in breach of the contract you signed with them
- Bonuses should be clearly tied to a measurement. If you pay a bonus, you need to explain what it's for
- We recommend that you do performance appraisals on a 6-month basis, followed by a salary review a month later. eg, if you review in March and in September, then you can review salaries in April, ready for your May budgets and costings for the next financial year
- Be conscious of the fact that it's never just about the money and that you need to keep fostering an environment of openness, feedback and good communication

## Track 8

### Tax Update

#### Michael Jones, Cummings Flavel McCormack

- Michael's 10-point action plan for those who have inadvertently overstepped their contribution limit into super:
  1. Identify all contributions made during the year (especially where there are multiple employers or defined benefit interests)
  2. Check for potential mis-reporting of contributions by super funds or errors in the individual's tax return
  3. Make sure contributions have been allocated to the correct financial year
  4. Apply to the Commissioner within the 60-day time limit to have certain contributions disregarded or reallocated to another financial year
  5. Check for any non-concessional contributions that are excluded under the exceptions for CGT small business assets and personal injury
  6. Avoid additional penalties by ensuring compliance within the time limits for giving a release authority to a super fund
  7. Use the release authority that will produce the best tax result under the future application of the proportioning rule
  8. Request that the super fund revises an incorrect Members Contribution Statement - or complain to the Superannuation Complaints Tribunal if the fund refuses to correct it
  9. If all else fails, consider objecting against the assessment

10. Put mechanisms in place to ensure the taxpayer does not exceed his or her contributions limits in future years
- Treasury has announced changes to the taxation of trust income that will apply from the 2011 income year
  - It will ensure that capital gains and franked income can be streamed to particular beneficiaries
  - It will align trust income with tax income

## **Track 9**

### **Sharemarket Update**

**Elio D'Amato, Lincoln Stock Doctor**

- On the plus side, the Chinese economy continues to prosper as evidenced during their latest five-year planning conference, and that's good news for Australia
- In the recent reporting season, major stocks that met expectations included Commonwealth Bank; BHP Billiton; Adelaide Brighton, a construction materials firm, and Boral
- On the downside, Seek, Bluescope Steel and Myer Holdings all disappointed and their share prices dropped
- Our list of Star Stocks is growing, which indicates that the Australian economy and the companies within it are generally doing quite well
- Twenty-three stocks remained on the list, and a very impressive 30 came in, ranging from the

big miners to Flight Centre and a small IT company

- Ten dropped out, including the much-loved CSL and Woolworths. Several were close candidates, but the rules are strict
- If you're considering selling stocks, look at why you got into them in the first place. Are they a short-term or long-term holding? Did you buy for income, which now may be falling short?
- To help you decide, read company announcements, including the latest financial report, and talk to a broker or advisor like Stock Doctor
- If you're no longer comfortable with the stock, sell, because you may be missing out on other, much better opportunities
- We're still in a two-speed economy: mining and engineering services are outstripping manufacturing and the industrial sector. It's hard to find winners there

## **Track 10**

### **Polish Up Your Presentations Skills**

**Andrew Griffiths**

- Take the time to really think about your presentation and what you wish to achieve
- Make sure you've done your homework beforehand - it makes a huge difference
- Structure your presentation, think about your opening words (the problem), outline how you can help, what the audience needs to do
- Always arrive early and scope out the venue
- Plan for problems, they're bound to arise

- Have a scalable presentation so that it's easy to reduce if your time is curtailed
- Beware death by PowerPoint - keep PowerPoint visuals simple, you are the main act
- Become a great storyteller - people may forget facts and figures but they'll remember stories long after the event
- Rehearse, rehearse, rehearse
- Learn from others - great or poor
- Avoid coffee or alcohol - a few stiff drinks beforehand are not the way to improve your presentation
- Remember one very important fact: the audience is on your side
- The more you present, the better you'll get