

The Calculated Exit

M&A UPDATE | VOL 1

presented by:



Welcome to the summer 2021 edition of The Calculated Exit. Here you will find observations and opinions related to M&A activity as seen through the lens of a boutique transaction advisory group.

DEAL ACTIVITY

Our transaction advisory team has seen an active 2020 deal climate grow substantially in 2021. We have assisted several 2021 deal closings with dozens still in process. Momentum in deal activity continues to occur as we enter the first few weeks of Q3.

VALUATIONS

Valuations have generally continued to be strong with little to no decrease in valuation multiples and buyer appetite. Some sectors have seen an increase in both over the past 12 months. Cash surpluses and public and private sector pressure on returns continues to fuel acquisition deal flow as does proposed tax legislation.

SPRINT TO THE FINISH?

There seems to be momentum building around the ticking tax legislation clock. Popular opinion sees a capital gains tax rate increase looming in the near future (or not so distant past if retroactive in nature). We feel that a tax rate hike is more likely than not, but that a retroactive rate hike is much less likely. A conservative view is that of a potential January 1, 2022 capital gain tax rate hike.

WHAT WOULD A TAX RATE INCREASE DO?

If the long-term capital gain tax rate increases from 20% to 39.6%, as is the desire of President Biden, this would have a substantial impact on net cash flow to our sellers. A business owner would have to increase the sale price by almost 33% just to break even on the additional income taxes due on the transaction. See the example below:

	Net Gain on Sale	Federal Tax	Net Cash to Seller	Net Cash Lost
Current Rate 20%	\$10,000,000	\$2,000,000	\$8,000,000	
Proposed Rate 39.6%	\$10,000,000	\$3,960,000	\$6,040,000	\$1,960,000
Premium Required 32.45%	\$13,245,033	\$5,245,033	\$8,000,000	Same net cash

Note: the example above is simplified for illustration purposes, and ignores possible net investment income tax, alternative minimum tax, and state level taxes.

Consequently, Q4 deal flow is expected to reach frenzied levels.

DON'T LET THE TAX TAIL WAG THE DOG

When the time is right, you will know it. Hopefully you will know with a year or more to plan properly. Don't let "possible" tax law changes push you into a knee-jerk reaction of selling your unprepared business to the highest available bidder. Start planning now and you will be more likely to optimize your business' value when it's time to sell.

“Deal flow is gaining even more momentum and is expected to reach a frenzy in Q4”

THE LONGER VIEW

Now is the time to plan and strategically enhance your enterprise value by driving EBITDA, cutting your costs, and enhancing existing margins. Our team is currently working with several M&A clients on both the seller and buyer side. In many cases, it can take years of planning and fine tuning to properly position your business for a successful exit. We have found that business owners who plan ahead to avoid the “fire sale” are overwhelmingly more successful in the end. Success is measured by overall transaction value of course.

THINKING OF SELLING YOUR BUSINESS?

Selling your business is a process, not an event. Determining the right time to sell, and finding the right buyer to sell to, can be stressful. There are legal and tax issues to consider, and negotiations can be complex and lengthy.

CRR CAN HELP.

Whether you need help buying, selling, merging, or handing down your business, we can help guide you through the entire process, from preliminary negotiations to post-closing adjustments.



MEET THE EXPERT.

David has been a member of the firm since inception and has been practicing in public accounting for more than 25 years. As the head of the firm’s Transaction Advisory Group, he regularly advises CRR clients in buying and selling their businesses, as well as mergers, acquisitions, and joint ventures.

David’s skill set is valuable throughout all stages of the transaction process, and through early involvement he is able to help maximize the financial results for his clients. His tactical approach to buyer and seller due diligence enables a smooth transaction process, with a focus on facilitating a well-organized transition for both sides. He also frequently speaks and writes on these topics and hosts transaction related seminars and workshops.



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