GREATER NASHVILLE

2017

Exit Planning Institute

A LOCAL MARKET STUDY:

The State of Owner Readiness

BENCHMARKING LOWER MIDDLE MARKET BUSINESSES AND EDUCATING OWNERS ON THE DIFFERENCES OF "ATTRACTIVENESS" VERSUS "READINESS"

IN PARTNERSHIP WITH

BNY MELLON
WEALTH MANAGEMENT

As a Wealth Director and Certified Exit Planning Advisor with BNY Mellon, I've spent many years collaborating with business owners on countless transitions. Having partnered with individuals as they prepare to leave a business that has been their life's work, I've seen the ways this process can go smoothly—and ways it can be difficult at every step. This "State of Owner Readiness" survey conducted by Vanderbilt University's Owens School of Management, underscores the importance of proper planning, professional guidance and preparation well in advance of a successful business transition.

I've heard many stories of difficult transitions and the regret that some owners feel after they've sold their business. Those stories fuel my passion for helping business owners. Take, for example, a business that had been in the family for three generations. Both spouses actively worked in the business. When the time came for the owners to consider transitioning out of their business, they weren't adequately prepared for the sale process or life after the sale.

Prior to engaging any offers, the owners had done very little estate planning. It wasn't until an offer came in that they started thinking about tax saving, an efficient wealth transfer to their family, and all the other issues involved in such a major transaction. Therefore, the sellers had a protracted period of due diligence. They hadn't established the solid accounting practices needed to substantiate their earnings and performance claims behind their company valuation. Furthermore, because the business was owner dependent and lacked a strong management team, the company lost value as the owners focused on the sales negotiations and lost sight of running the day to day business. As a result, the buyers ultimately reduced their offer by 35%.

Meanwhile, the owners, who were focused on charitable giving, wanted to establish a private foundation in addition to setting up trusts for their children. But they hadn't given enough thought to their own financial needs. It wasn't until 14 hours before closing the sale that they asked, "Will we have enough to meet our spending needs, charitable goals and gifting for the family?" Fortunately for this family, the answer was yes; the offer was sufficient to cover these different objectives. But in many cases, especially at the last minute, the answer is no.

Because the final sale price was so much lower, the buyers agreed to performance clauses that allowed the owners to recoup some of that loss. However, the arrangement soured quickly. The former owners struggled with giving up control to a new board and chafed at the loss of standing with their employees and vendors. Two months into their new employment agreement they resigned, forgoing the large earn out. A year later, the owners expressed extreme regret that they sold. Their company had been the main focus of their life, and it was how they identified themselves in the community. They had never traveled, developed hobbies or thought about life after the business. Without it, they felt lost and depressed.

In addition, turning the value of their business into a large sum of money to be managed and invested continues to be difficult. The owners had always felt in control of their future through the success of the company. But now they have to put their trust in the capital markets where they anxiously watch their net worth fluctuate throughout the day with the major indexes like the Dow, S&P and NASDAQ. Each market drop feels like an actual loss of the time, energy and resources they devoted to building their business and wealth over the years.

In the coming decade we can expect business transitions to grow steadily along with demand for advisors whose expertise is in working with business owners. Baby boomers reportedly own over 60% of closely held businesses today, according to the Exit Planning Institute. Most business owners have a significant portion of their total net worth tied up in their business and will require a successful transition to meet their future financial goals and objectives. The Exit Planning Institute conducted a study suggesting as high as 80% of these companies are not saleable with the team of advisors the owners have in place. As the business owners' companies grow in size and complexity, often their advisors haven't changed and thus may not be the right team of professionals for tax preparation, estate planning, cash flow analysis, exit/succession planning or wealth management.

In addition to assembling the right team of advisors long before it's time to sell, owners need to ensure they work together to avoid offering conflicting advice for the business owner. Owners should select one primary advisor or firm to take the lead and hold annual team meetings to discuss goals and planning opportunities so that they can ensure they are working together.

Insufficient planning can have serious—if not disastrous—consequences and I've made it my mission to find a better path for business owners. I want to help individuals and families maximize the value of their business and avoid costly mistakes. Equally as important, I aim to ensure that these business owners are prepared emotionally for the next phase of their lives.

This report further illustrates how owners who plan ahead are more likely to receive the best value for their business, limit their tax liability and experience a smooth transition into a new chapter in their personal lives. The "State Owner Readiness" survey will reinforce that it's never too early to start!

Gary Rzucidlo, CEPA
Vice President, Senior Wealth Director, BNY Mellon Wealth Management

THE STATE OF OWNER READINESS
2017 GREATER NASHVILLE REPORT

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Table of Contents

Survey Overview

In 2016, the Exit Planning Institute (EPI), in partnership with BNY Mellon Wealth Management and Vanderbilt University's Owen Graduate School of Management, conducted a survey of business owners in the Greater Nashville region to determine their state of readiness to transition their businesses and unlock the wealth accumulated in the business. Additionally, we wanted to compare the Greater Nashville results to EPI's national survey. Last, we wanted to point out specific things that owners who are successful do versus those who are not and offer suggestions to business owners and business advisors regarding what they can do to improve the probability of a successful transition and unlock this vast wealth.

There are roughly six million operating privately held companies in the US. They represent approximately $30 trillion in sales. According to US census data, 63% of these are owned by Baby Boomers who now range from 53-71 years old with the average age being 62. Although Baby Boomers are holding on to their businesses for a longer period of time, all Boomers will reach the age of 70 or older within 17 years. That represents nearly 4 million Baby Boomer businesses poised to transition. Assuming a business valuation of 50% of sales, reasonable by most standards, that further represents $10 trillion of wealth poised to transition.

Unlocking this wealth in the business is or should be of paramount importance to all business owners if for no other reason that **most owners have 80-90% of their financial assets located in the business itself**. Given the significance of this asset in the owner's wealth portfolio, the ability to monetize this wealth at some point will have a significant impact on the owner's financial security and lifestyle once they exit the business.

The significance of the business asset transition goes beyond the owner and owner's family. Failure to provide for the continuity of the business not only affects the owner's personal wealth for his or her family, but for all other stakeholders who depend on the successful transition of the business. "The business owner is the giver of life" wrote Leon Danco, a legendary expert on family businesses, in his book entitled Beyond Survival, a Guide for Business Owners and Their Families. With roughly 6 million operating privately held companies in the US representing around $30 trillion in sales and $15 trillion in wealth, the continuity of the owner's business matters not just to his or her family, but to the employees, vendors, customers, charities and the communities where the owner provides jobs and economic and social well-being for the business' local community.

What happens if the business does not successfully transition? The alternative is that the business shuts down. People lose their jobs. Families suffer. Communities suffer. And in many cases an owner's life's work is liquidated for pennies on the dollar.

Previous surveys conducted by EPI, Price Waterhouse Coopers (PWC), the Alliance of Mergers and Acquisitions (AM&AA), Tom West, founder of Business Broker Press, and the Family Firm Institute (FFI), have determined that historical transition success rates are in the range of only 20-30% nationally.

The mission of BNY Mellon, the Exit Planning Institute and all Certified Exit Planning Advisors (CEPA) worldwide is to change this outcome. The beauty is that we have models (after all, 20-30% of businesses do successfully transition) which can be emulated by many business owners who decide that a successful business transition is in their future.

The significance of this is becoming more urgent as Baby Boomers, who own nearly two-thirds of all privately held businesses, face the inevitable condition of aging. Boomer owned businesses alone represent roughly $20 trillion in sales and $10 trillion of wealth in the US alone. Even though Boomers are holding onto their business longer than previous generations, they must face the reality that preparing for their business transition is now an urgent imperative.

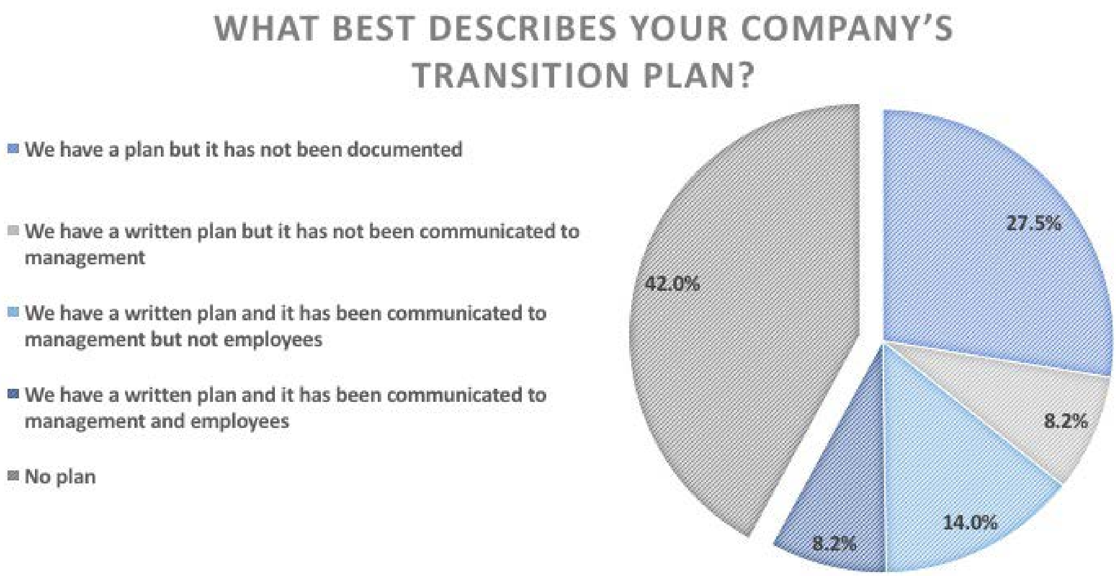
The community of owners must realize that transitioning a business is a high stakes, and for many, a once-in-a-lifetime endeavor that takes significant focus, action, and time to do it properly.

Doing it right has crucial benefits. For many owners, the business represents the vast majority of their wealth. For example, if the average middle market business, which we define as a business with sales between $5 and $100 million, holding a market value of $8.5 million, successfully transitions, the wealth at transition goes from $2.1 million in wealth to $10.6million in pre-tax wealth. Even at an aggressive rate of return of 6% a year, the difference in pre-tax income is $510,000 ($637,000 vs $127,000) per year.

For the micro market, the consequences are even more compelling. In the micro market, which we define as those businesses that do less than $5 million in sales per year, the average business value is just over $300,000. Most of these businesses are owner operated, meaning the owner derives almost all income from the business. Roughly 5.7 million (94%) of the 6 million privately held businesses fall into this category. Assuming again that for many 80% of their wealth is locked in the business, successfully monetizing the business asset is the difference between having $400,000 at transition as opposed to $100,000.

To successfully transition, three things must be addressed by the owner: 1) the owner must focus on maximizing transferrable business value for as long as they hold it while positioning it to successfully transfer upon exit so they can harvest wealth locked in the business; 2) the owner must prepare financially for a lifestyle without the income from the business; and 3) the owner must plan personally for what they will do (their third act) after exiting the business.

To understand the present level of readiness to harvest this wealth, the current financial preparedness outside the business financially and understand how well owners have prepared personally, EPI has been conducting surveys of business owners with the help of its many strategic partners since 2013. National surveys were completed in 2013 and 2014. Two regional surveys were conducted in 2016 and several more regional surveys are planned in 2017.



Shown above: 42% of owners have NO transition plan AT ALL!

The survey results continue to demonstrate the lack of readiness to transition by many business owners which explains why most transitions fail. The report also demonstrates the need for massive education of business owners and business advisors with regard to how to successfully transition.

It is important for the reader to note that the survey answers reflect the owner's *perception*. Although the owner's answer may be factual, it is not based on proven fact. The only way this can be accomplished is through the completion of a thorough personal, financial and business assessment conducted by an independent credentialed advisor, such as a CEPA.

Nevertheless, the data is useful to at least assess the *owner's state of mind* as it relates to being ready to transition from a business, personal and financial standpoint. Owners would be wise to consider obtaining a personal, financial and business assessment to support their current perceptions and their business valuation. The owner will then avoid surprises when the time comes to transition the business. This is also necessary for proper estate and personal financial planning.

As stated earlier, we know from past studies that success rates in the US are in the range of 20-30% - far below what we need them to be from an economic and social standpoint. Some of the owner's responses in these studies reflect good reasons for why that is. Other answers may reflect an owner's misunderstanding or under estimation of what it takes to successfully transition. In other words, it may simply be that owners don't know what they don't know. Their lack of formal education certainly demonstrates that they have not accomplished enough education.

The intent for this data is that it be used as a business tool to discuss with the owner and to identify areas where education and services are needed. At minimum, the results should be reviewed with business owners to begin the process of validating their particular situation, educating them on critical success factors, and determining the probability of successful transition.

This report is divided in to three sections. In Section 1, we make general observations about the data collected from the Greater Nashville survey and compare it to the national surveys conducted by EPI in 2013 and 2014. In Section 2, we provide analysis of the data and make observations as to what it means to the business owner. In Section 3, we recommend actions business owners and business advisors should take to improve the probability of a successful transition and capture this hard-earned wealth.

8,398 surveys were distributed with 222 responses (2.64%). The survey included 50 questions organized as follows:

- demographic information (age, gender, annual revenue, legal structure, industry, most trusted advisor, etc.);
- current transition plans and thoughts; and
- owner, shareholder and family readiness to transition, and company readiness to transition.

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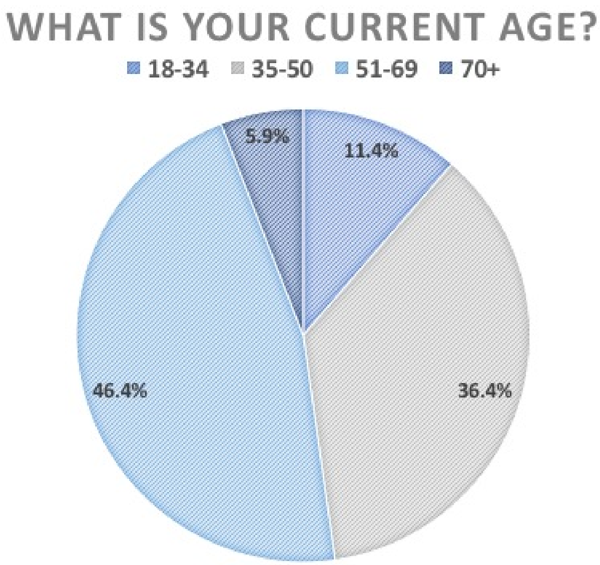
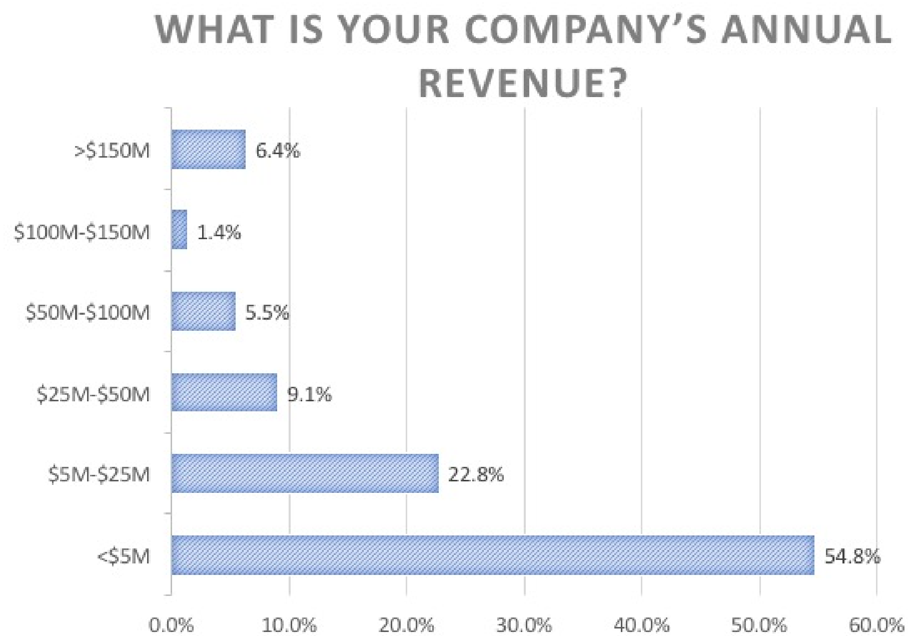
Section One: Demographic Data

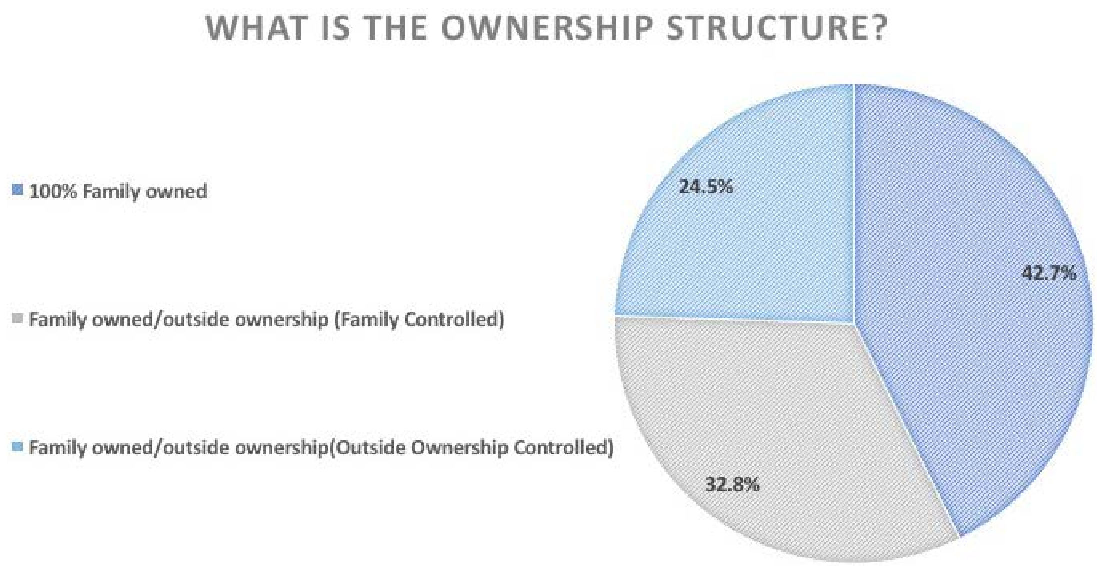
What Our Owners Look Like



- Owners Ages: 46% of the respondents were Baby Boomers. The Greater Nashville sample of businesses resulted in an audience that was younger on average than US Census data which indicates 63% of privately held businesses are owned by Baby Boomers. 52% of the Nashville sample were 51 years of age or older. The importance of transition significantly rises as the owner ages meaning it is highly likely that the successful transition of the owners most valuable asset, the business, should be a high priority for 116 of the 222 owners surveyed.



- Business Size: 55% had business sales of less than $5 million, 37% had sales in the range of $5-100 million, and 8% had sales of $100 million or more. The Greater Nashville data leans more heavily towards businesses over $5 million in sales versus the national US Census data which states that of the six million privately held operating companies, 94% do $5 million in sales or less, 5.8% between $5 million to $100 million, and only .2% do over $100 million in sales.



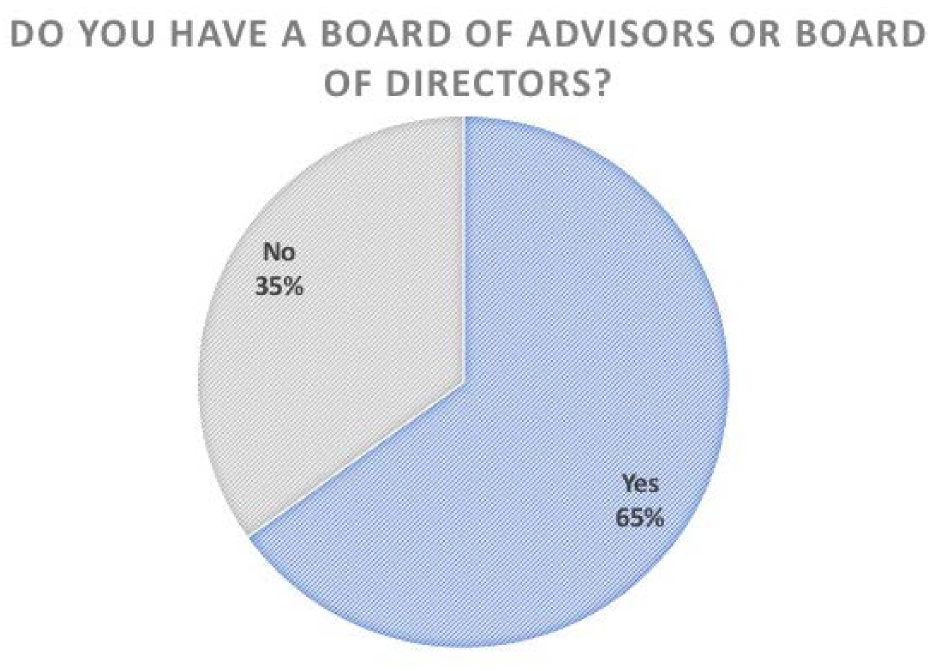
- Family Ownership: Only 41% were family owned businesses (although 76% were family controlled) with 85% of the businesses being first generation businesses most likely started by the owner. This sample had a greater degree of outside ownership. However, given that 76% of the sample was family controlled, we still believe the data aligns with a Family Firm Institute study which indicated that only 30% of businesses that transition from generation 1 to generation 2 are successful, and it gets progressively worse from there.

We believe that the above demographic differences are relevant to the study results which generally found that the Nashville sample business owners have a greater perception of being "ready" to transition their businesses. The audience on average was younger, included larger businesses and had a greater degree of outside ownership than in previous surveys.

> Nashville business owners have a greater perception of being "ready."

The Exit Planning Institute has found through informal interactions with owners who participate in its chapter events that younger owners are more receptive to the concepts of exit planning which is contrary to what the reader might assume. EPI has learned that younger owners tend to view "exit" as a step to monetize their investment and since they are younger, view the exit process as a means to "cash out" so they can do it again. By contrast, older owners, particularly Baby Boomers, tend to view the exit as their last hurrah, and have greater issues due to lack of personal planning regarding what they will do next and greater fear of the loss of their identity, which is more closely aligned with the business itself.

Bear in mind that although the sample average age was younger than in previous surveys, Baby Boomer or older business owners still represent over half of the Greater Nashville sample.

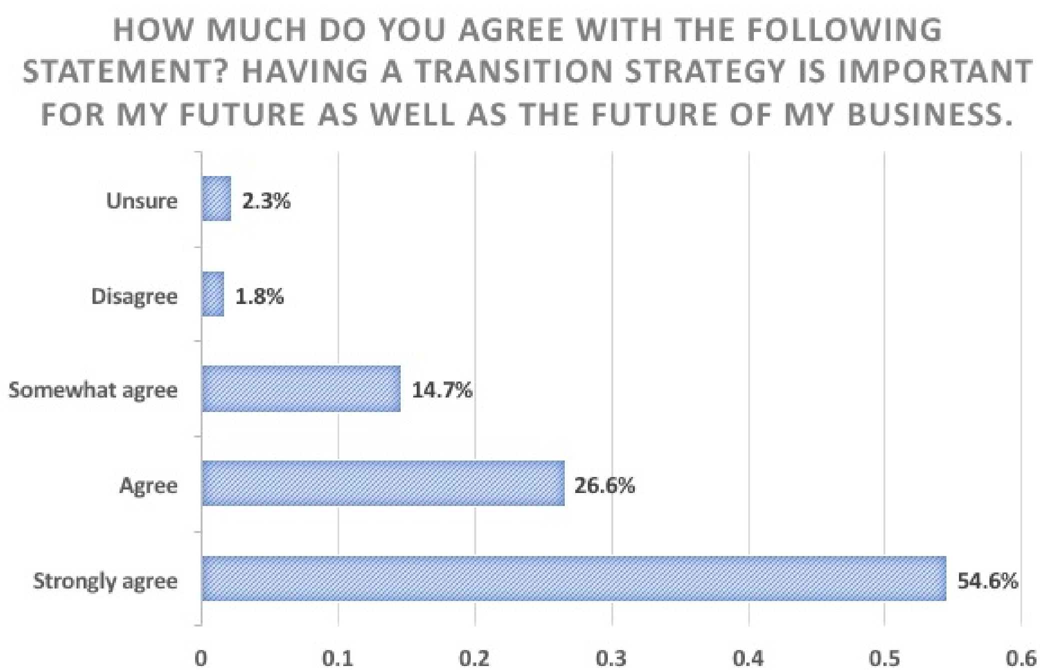


The Nashville sample had greater influence of outside resources, particularly the use of a board of advisors that included non-family members. We conclude that this is directly related to the fact that the sample more heavily represented a larger average business size than overall US Census data. Larger businesses have a tendency to include a greater use of outside, non-family, advisors which we believe is a valuable positive influence to the owners focus on value creation versus the business simply supporting the owner's lifestyle.

Section Two: Analysis and Relevant Observations

What does it all mean?

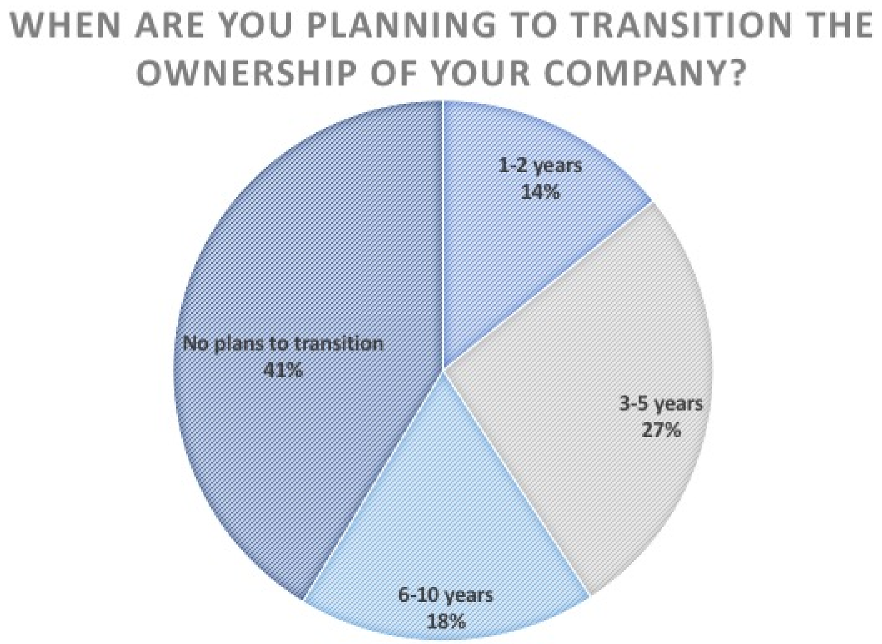
As you read through the rest of this report, the reader should bear in mind the following:



96% of the business owners indicated they agreed with this statement: "Having a transition strategy is important for my future as well as the future of the business."

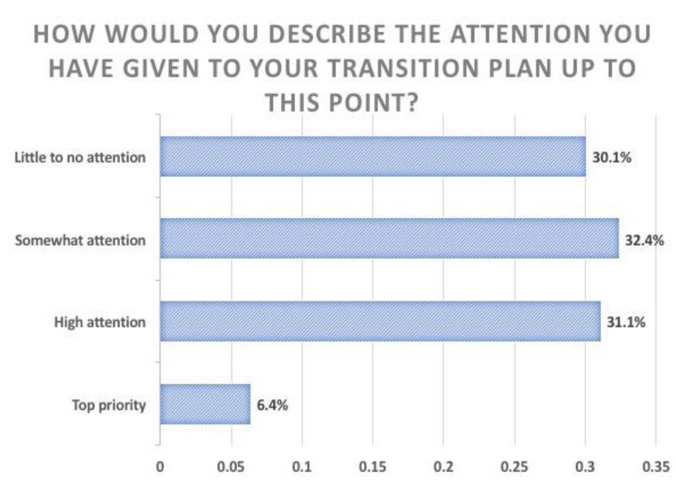
The fact that 96% of the owners who responded to the survey feel this way clearly correlates with our conclusion that although there is certainly room for improvements, in general, **the Greater Nashville sample of business owners have internalized the value of having a transition strategy. Overall, they feel more prepared to transition their businesses than in previous surveys completed by the Exit Planning Institute.** The following observations bear this out.

State of Transition Planning is stronger in the Nashville area although there is still room for improvement.



41% of the owners indicated they had "no plans" to transition their business. 41% indicated they were planning to transition within 5 years and 59% within 10 years.

Only 30% stated they had given little to no attention to their transition at this point. 37% had given it high to top priority and 70% at least some attention. This is very relevant. Previous surveys indicated little to no attention above 50% and high or top priority at 14%. This demonstrates that the Nashville sample of business owners much more actively integrate transition strategy into the way they operate their businesses.



- Although only 30% indicated they had a *written* transition plan, this is better than previous surveys which were in the range of only 12%-17%. 42% said they had no plan at all which is in line with 49% in national survey. 28% said they had a plan but it was not written nor communicated.

- Despite more owners having written transition plans in the Nashville area, which is a good thing, confidentiality is still paramount. The owners do not feel that the plan needs to be shared with management and employees. Only 8% stated they had a formal written plan that had been communicated to both management and employees.

- Despite the lack of communication of a written transition plan, 69% of the business owners indicated they were at least somewhat comfortable their managerial team (as compared to 55% in a previous survey in another region) would be successful If they were not involved with the business post transition. 51% (vs. 25% in a previous survey in another region) indicated they were very comfortable. Only 21% indicated they had not even thought about management succession.

Business Valuation and Value Enhancement: A Cornerstone for Exit Planning

WHAT DO YOU WANT TO ACCOMPLISH AS PART OF THE TRANSFER OF YOUR BUSINESS?

(MOST IMPORTANT TO LEAST IMPORTANT)

1	GET FULL VALUE FOR MY BUSINESS
2	MAINTAIN THE LONG-TERM VIABILITY OF THE BUSINESS
3	PROVIDE BENEFIT TO MY MANAGER AND EMPLOYEES
4	MINIMIZE OR ELIMINATE CAPITAL GAINS TAX
5	TRANSFER WEALTH TO MY CHILDREN OR GRANDCHILDREN

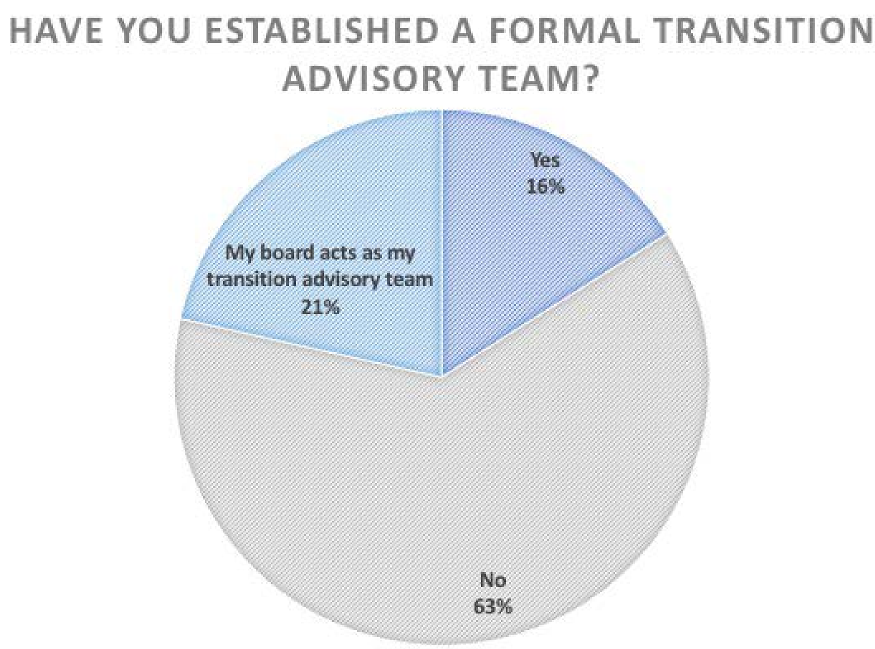
57% of the owners said that "Getting full value for my business to fund my retirement or other business interests" was their number 1 goal in the transition of the business. This aligns with previous surveys.

- Given that more owners had developed transition plans, it was not surprising to see that transitions plans were more inclusive across the board.
- 85% of the business owners indicated their transition plans include a business valuation, 60% included contingency planning, 46% included a tax plan.
- 32% of those that had a plan said their plan included value enhancement. Although we would like to see this percentage much higher, 32% is much better than previous surveys where only 13-19% of the owners said their transition plans included value enhancement.
- 47% have completed a formal valuation of the business in the last year and 76% have had a formal valuation in the last three years. This is much better than in previous surveys where we have seen this number below 40%.
- 53% have never had their financial statements audited. However, Nashville had a larger group (34%) who indicated they had audited financial statements within the last year. Again, we believe this is directly related to the sample including larger businesses.

Significantly Greater Use of Outside Resources. Greater Role of a Board of Advisors

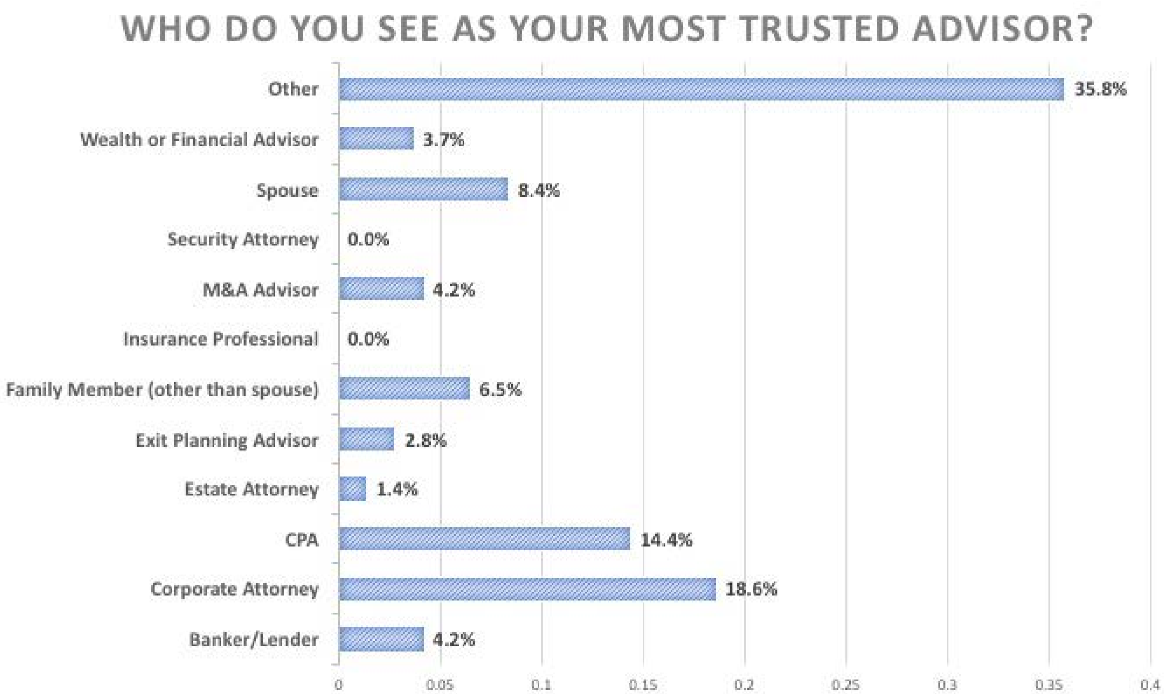
It was clear from the Greater Nashville owner sample that the use of outside resources is more common. Most notably, the board of advisors plays a much bigger role in the owner's business life. This may be due to the sample being younger and typically larger in size than in previous surveys.

- 53% have sought outside advice. Although we would like to see this be bigger, this compares to only 20% in a previous survey in another region. The number 1 reason they had not sought outside advice was that they were still building value. This aligns with the greater number of owners that included value enhancement as part of their transition planning and in general indicates a greater understanding of the importance of focusing on value growth to transition planning. Exit strategy is nothing more than good business strategy. Focusing on value as a primary business goal produces all other positive outcomes. The owners in the Greater Nashville area appear to be more receptive to this concept.

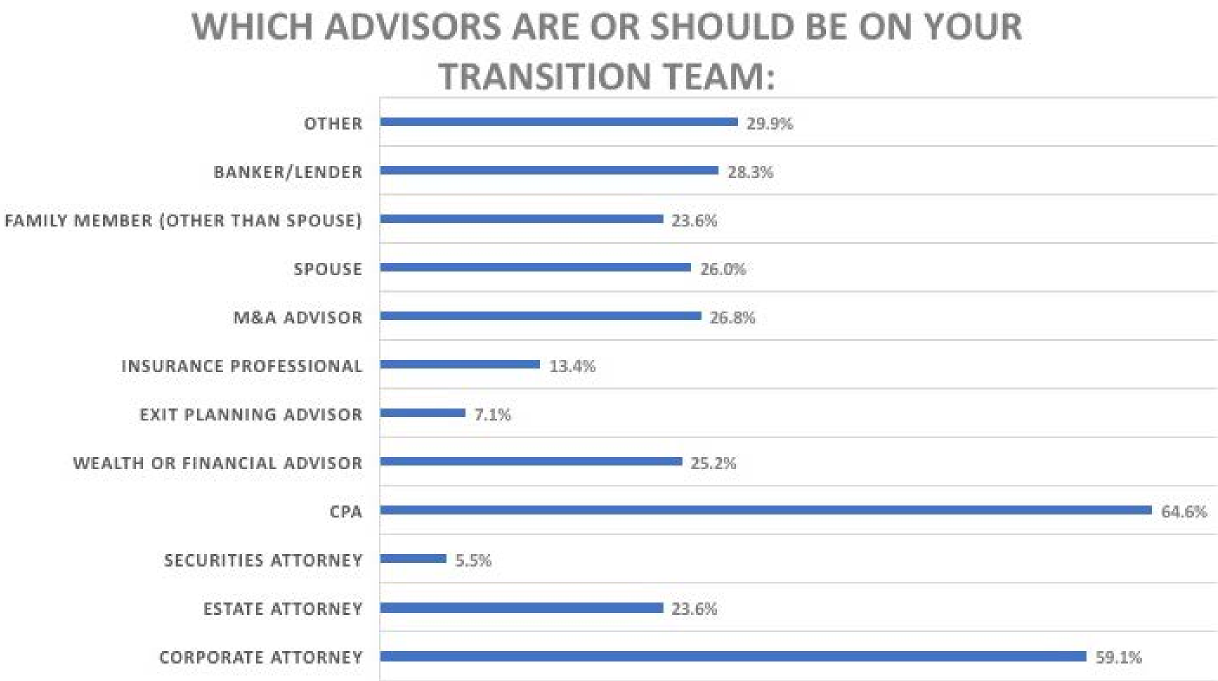


- 63% indicated they have not set up a formal transition team. 21% indicated their board was acting in the role of their transition team. Typically, this is a mistake. Most advisors and many owners should realize that the skillsets needed to transition a business can be much different than those skillsets of the members who sit on the owner's advisory board.

- **But the use of a board of advisors was much more likely amongst the Nashville business owners. 65% of the respondents have an outside board of advisors** in Nashville as compared to 20-28% in previous surveys. And it was much more likely that non-family members, outside of the business were active on the board. 50% of the business owners (as compared to 8-9% in previous surveys) indicated they had non-family members on the board of advisors.



- **The most trusted advisor status went to the corporate attorney vs. CPA in previous surveys.** Again, we believe this is directly related to the larger average business size and the overall stronger planning and focus on building business value. The CPA ranked #2 most trusted at 14%. The spouse was ranked at only 8% as compared to previous surveys where the spouse was named most trusted by 16-23% of the business owners.
- **"Other" was actually the highest ranking in terms of most trusted at 36%.** Owners were requested to write in the type of advisor if they answered "other." A scan of this write in data indicated that often the most trusted advisor for the Greater Nashville area business owner was a "board member" or "peer group."

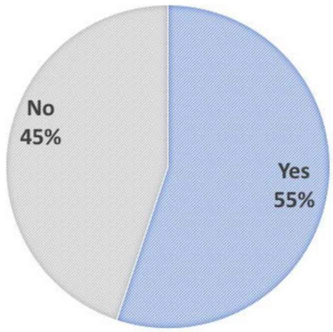


- 25% of the owners stated the wealth manager/financial planner should be or is on the transition team. Yet only 4% considered the wealth manager/financial planner the most trusted. This is clearly an opportunity for the wealth management and financial planning community.
    - *This is surprising and I believe is a huge opportunity for the financial planning industry. It is clearly a best practice to have a wealth manager or financial planner involved in the transition process as early as possible. I don't even know how it's possible to design a transition strategy without the involvement of the financial planner. The role of the financial planner is critical in determining the owner's financial needs before, during and after the exit. Their role in evaluating options to optimize the owner's post business lifestyle is critical and often dictates the available exit options, the structure of the exit transaction and internal or external option. The financial planning industry and owners themselves would benefit tremendously if the financial planning industry did a better job of educating owners on the role of the financial planner and wealth manager in the transition process.*

Big Concerns About the Accuracy of Estate and Personal Financial Plans

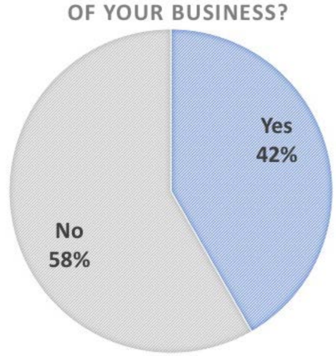
Despite all the positives of the Nashville study, the greater influence of outside resources and the use of a board of advisors, this area stood out as having the most need. There appears to be confusion over whether or not estate and financial planning is needed. Given the size of the business wealth built into the Nashville sample, 42% of the respondents said they did NOT have an estate plan. Although 58% said they did have an estate plan, there are significant concerns over its accuracy and the degree of preparedness. For the 58% that said they had an estate plan:

HAS YOUR ESTATE PLAN BEEN UPDATED IN THE LAST 2 YEARS?



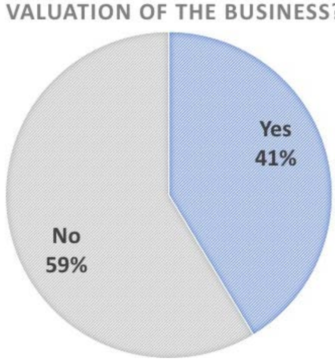
Only 55% said their estate plan had been updated in the last two years.

DOES YOUR ESTATE PLAN PROVIDE FOR THE SALE OF YOUR BUSINESS?

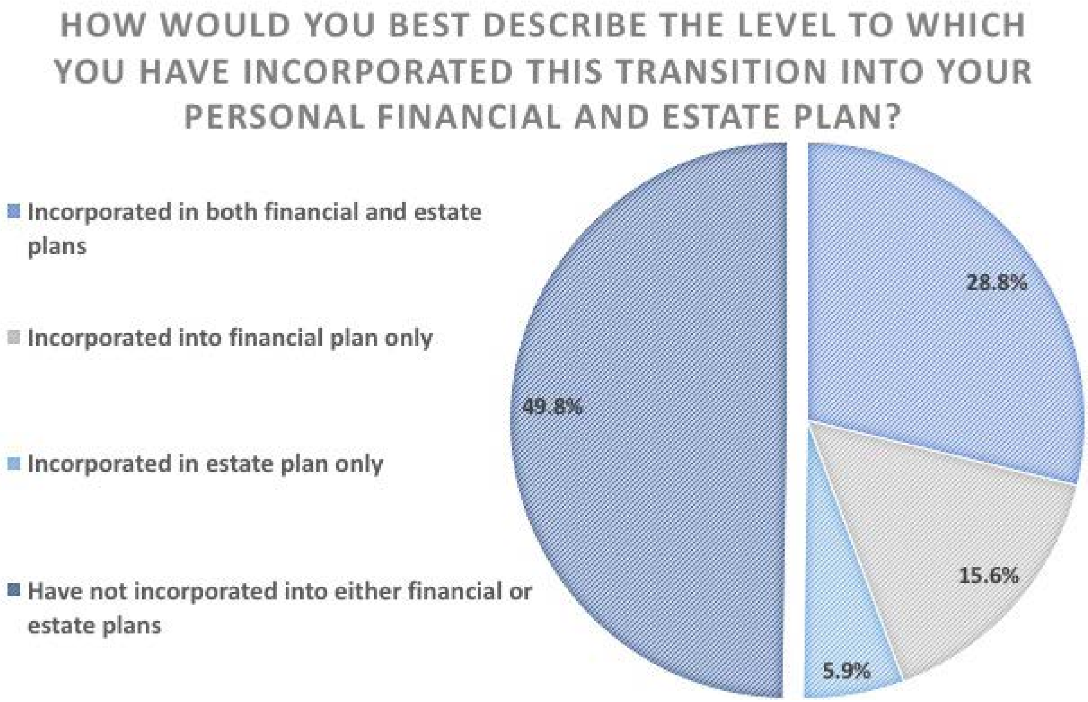


58% indicated their estate plan did NOT provide for the sale of their business.

DOES YOUR ESTATE PLAN INCLUDE AN UPDATED VALUATION OF THE BUSINESS?



59% indicated it did NOT include and updated business valuation.



- Half (50%) of the business owners indicated their transition plan had NOT been incorporated into either the financial or estate plan;
- 55% did not know how much they NEEDED (vs wanted) to net from the sale of the business; and
- 0nly 30% have a tax minimization plan; and less than half of those that did said it was updated.

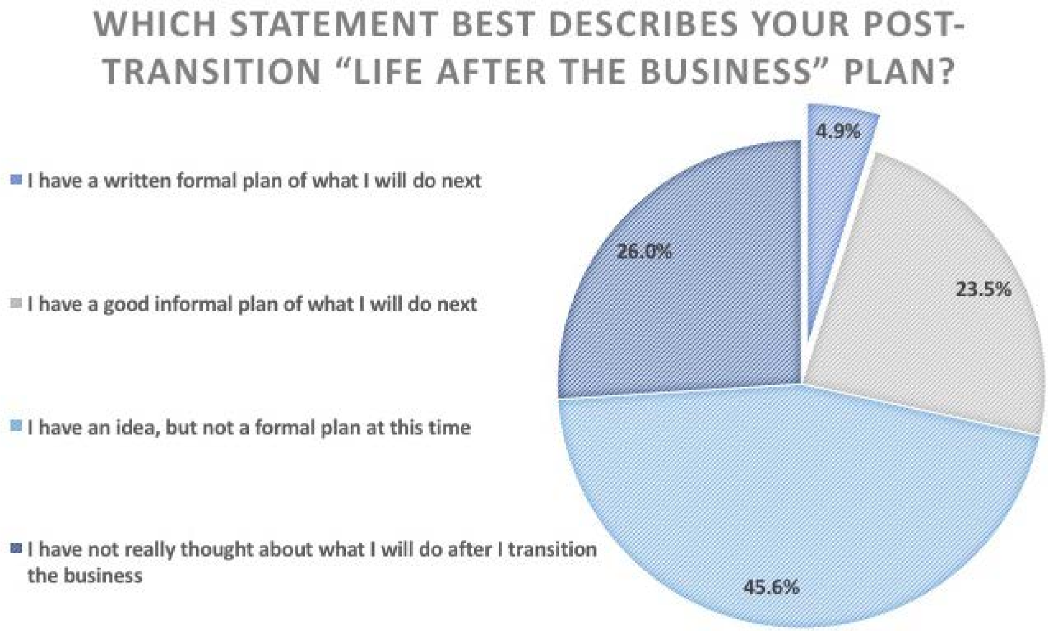
What is very worrisome is that the business transition and updated business valuation were not incorporated into the estate plans of a majority of those businesses that actually said they had one. If the business typically accounts for 80-90% of the owner's net worth, how can estate planning be effective when more than half of the business owners who have an estate plan have not incorporated the business transition into their plan, and there is limited tax and needs analysis completed?

Yet 57% answered that getting full value "for my business to fund my retirement or other business interests" was their number 1 goal in the transition of the business. More than half indicated they planned to transition the business in 10 years or less, and 41% said they were planning to transition the business in 5 years or less.

This appears to be another big opportunity for both owners and those that provide financial planning and estate planning services.

What's Next? The Third Act

Most Nashville owners do not have written personal plans for what they plan to do next. This is likely due to the fact that most owners indicated they were not planning to retire but rather invest in another business or serve on a board of advisors



The fact that only 5% of the owners indicated they had a written post-transition personal plan reflects an overly optimistic view of their future. When asked about the state of their post-transition personal plan.

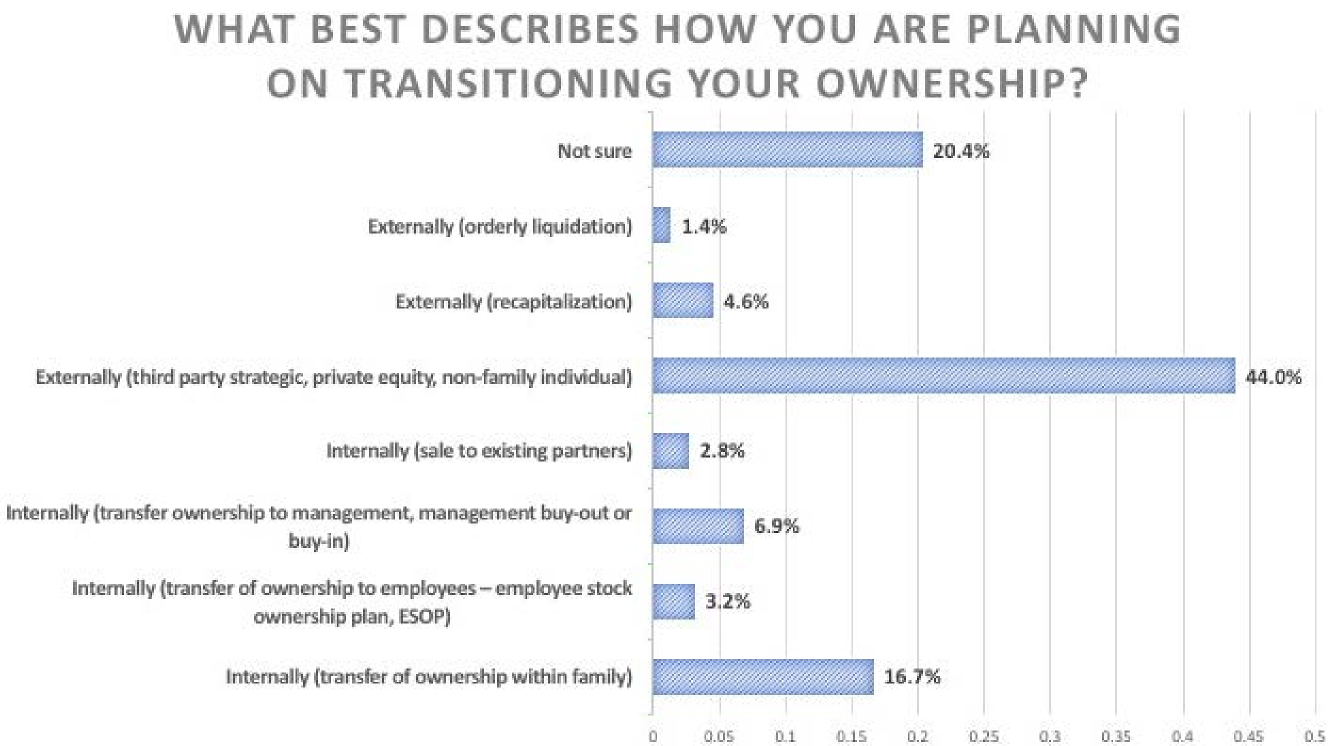
- 26% had not even thought about it.
- "I have an idea" was the most popular answer at 46%.

This is consistent with a Price Waterhouse Coopers study that indicated 75% of business owners surveyed within one year of exit profoundly regretted the decision. This was mainly for personal reasons; not financial reasons. An owner's identity is closely tied to his or her business. Losing that is the emotional equivalent of losing a close loved one. Owners spend untold hours working in and on their business. The owner's personal needs often take a back seat on the priority list.

However, this may be due to the younger average age of the sample. Many GenXers and millennials are not exiting for retirement purposes. They exit to monetize the value of the business and generally will re-invest that money into another business.

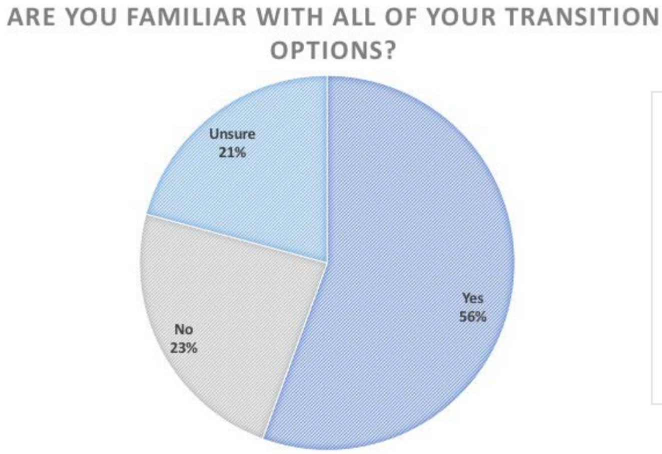
Only 11% of the sample indicated they were planning to retire post transition. Most (a strong 38%) said they were planning to invest in or serve on the board of another business.

Exit Options: Tennessee Owners Focused on Strategic Third Party Sales



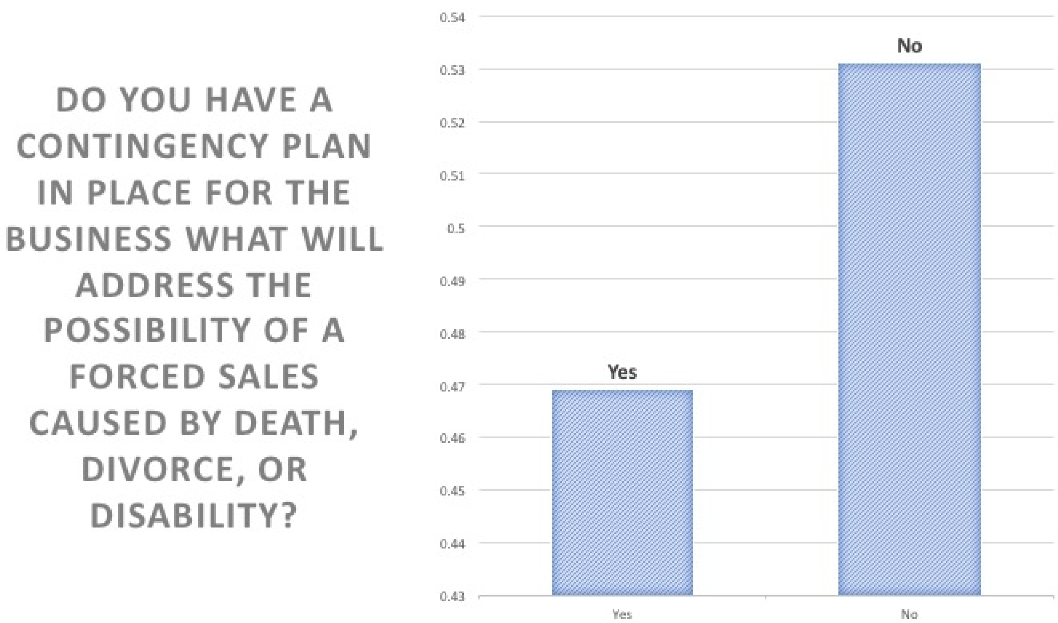
Owners are mainly focused on building value to position the business for a strategic sale to a third party. When asked, "What best describes how you are planning on transitioning your ownership?" **nearly half (44%) indicated they were planning a strategic sale**. Only 20% indicated they were "not sure."

- **The most popular inside option was to transition the business to a family member** (17%) followed by management (7%), and employees (3%) and partners (3%).
- **The most popular outside option was to sell to a third party including a strategic, private equity or non-family member** (44%), with only a small portion targeting an orderly liquidation (1%) or recap (5%)
- These data points are consistent with owners' previous answers indicating a greater focus on building value and the desire to invest in another business.



When asked if they were familiar with all their exit options, a strong 55% said yes. This is much better than previous surveys where 66-68% of business owners indicated they were not aware of all their exit options.

Business Risk Not Appropriately Addressed



53% of the owners indicated they have no contingency plan should they be forced into an exit. Of those that did say they have a contingency plan, only 60% have it documented. Given the other positive planning tendencies, active involvement of boards, and size of the companies in this sample, the fact that more than half of the sample indicated they do not have a contingency plan and only 60% that do have it documented, is a bit alarming.

Buy-Sell Agreements: Not Present or Not Up-to-Date

Of the businesses that have multiple partners, **31% do NOT have a written buy-sell agreement**. More than a third of those that do have a buy-sell agreement have NOT had it reviewed and updated within the last three years and 65% do not have it funded by life insurance.

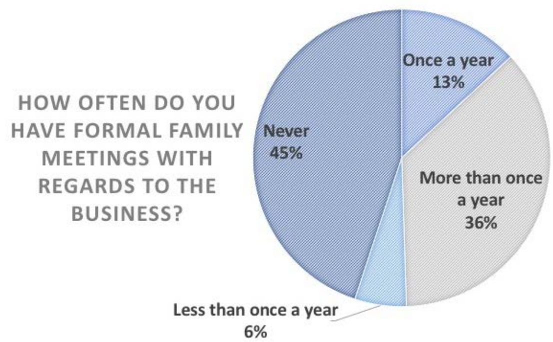
Family involvement in the transition process should be improved

Only 43% of the sample included businesses that were 100% family owned but 76% indicated the business was family controlled thereby demonstrating that family involvement is still significant.

Yet when asked to rank family readiness for the business to transition, **60% of the owners ranked the level family readiness incorporated into the transition plan below average**. And 45% said they have never held a formal family meeting about the business.

- This may be because 63% said family members would NOT be filling key positions and **only 17% indicated they had decided on a family transition as their preferred option**.

- If family members were filling key positions going forward, 60% answered these family members were at least somewhat ready but **40% indicated they were not ready at all**.

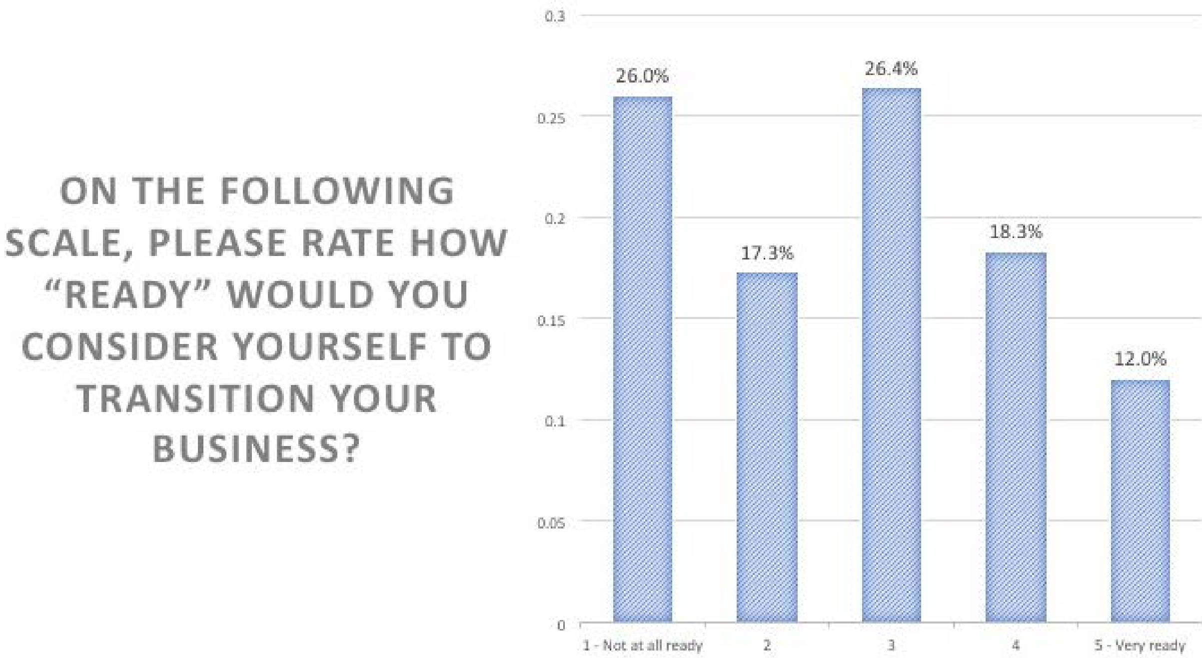


- For those that had incorporated family readiness into their transition plan, 52% indicated family members were aware of both managerial and ownership transition plans. Only 19% said they were not aware of either.

The danger here is that there is a tendency for business owners to do less transition planning when a decision has been made to transfer it to family. The family should approach the transition with the same vigor as if they were planning to sell to a third party, even if the family has decided on an inter-generational transfer. What makes a business valuable to a third party are the same characteristics that make it valuable to the next generation. One major reason we don't see success rates much higher for family transitions versus third party sales is because some owners do not approach the family transition in the same way they would approach a third-party sale and they end up transitioning a business to a less experienced family member (child) who is undercapitalized and has not mitigated risk appropriately. Even if the family will not be involved in the business (because the owners sells it to a third party), the family is still significantly affected.

Section Three: Recommended Actions

Advice to Business Owners



The results of the Greater Nashville study are more positive when compared to previous surveys. When asked to rank how **ready they felt the business** was to transition, 40% indicated above average and 70% indicated at least average. This compares to less than 50% in previous surveys. When asked to rank how **personally ready** they were to transition their business, however, only 30% felt they were above average and 56% answered average or above. **26% indicated they were "not personally ready at all."**

One would be safe to conclude that the owners in this survey have the perception that their businesses are better prepared. This perception is supported from their survey answers. They indicate owners have a greater focus on building value, are more aware of exit options, use more outside resources for guidance, and do a better job of integrating exit planning into business operations today. These are all very positive tendencies.

> "(Owners) have the perception that their businesses are better prepared."

The greatest weaknesses appear to be more in the realm of personal planning, which includes poor estate planning and financial planning, lack of sufficient attention to managing business risk, not updating buy-sell agreements, no development of written plans for what they plan to do next and lack of or poor communication with key family members.

As noted in the beginning of this report, it is important for you, the owner, to note that the survey answers reflect your *perception* of attractiveness and readiness. Your answers may be factual, but unless you have completed a thorough personal, financial and business assessment conducted by an independent credentialed advisor, such as a CEPA, and correlate these results to your business valuation, they are not based on proven fact.

> "Exit planning is a state of fact – not a state of mind."

Exit planning is a state of fact – not a state of mind. Unless you have evidence of your accomplishments, which you have built through structural capital (read about the 4Cs in *Walking to Destiny: 11 Actions An Owner Must Take To Rapidly Grow Value & Unlock Wealth*), you run the risk of trying to transition a business that is attractive, but not ready. Understand the difference between attractiveness and readiness. Your business may look attractive from the outside perspective, but is it transferrable? Taking an attractive business to market that is not ready to transition runs the risk of never making it through due diligence to completion of the sale or facing modified, less attractive offers and terms than were originally in the Letter of Intent. Owners should bear in mind that studies have shown that only 20% of the businesses that go to market actually sell; 80% do not. Many times, the reason for this is that the business may have appeared attractive, but was not ready to transition. You should also consider that personal readiness does have an impact on the value your business, certainly from a buyer's point of view.

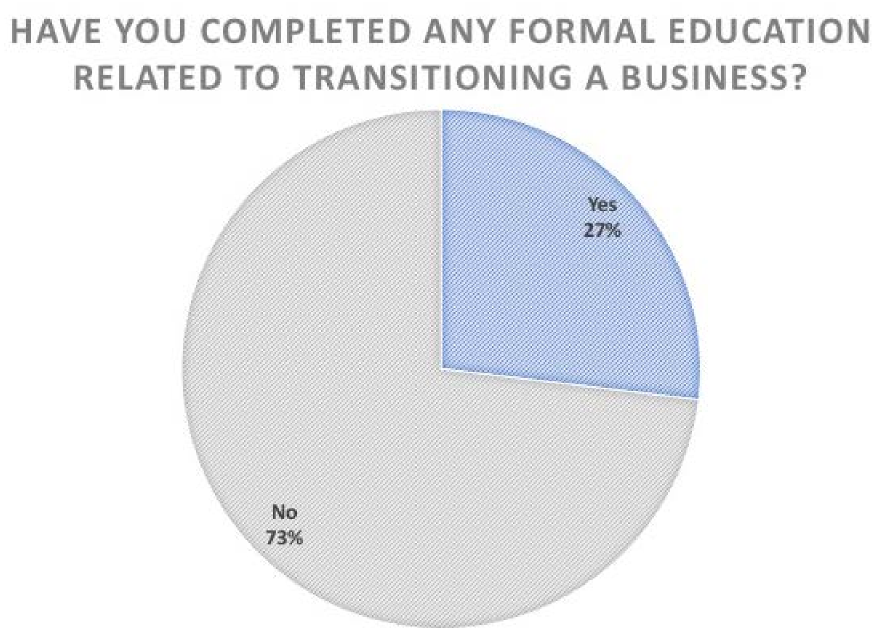
Exit planning is important because 80-90% of your net worth is likely to be locked up in your business. 70-80% of that business wealth is tied to intangible assets. To check this, owners need only look at their present income statements and balance sheets. Does the income produced on the income statement (for tax purposes) really reflect the true cash flow benefit assumed by the owner or future owner? The answer is often no when the owner considers normalized income and expenses, discretionary expenses charged to the business and one-time non-recurring charges. Does the owner's present balance sheet reflect the true "market value" of the business? Again, not often. The balance sheet (again for tax purposes) reflects the book value of the owner's written down business assets; not the true market value which would include the value of the business' intangible assets.

> "Does the owner's present balance sheet reflect the true "market value" of the business?"

Your management systems must be adapted to provide you strategy and feedback on the value of *transferable* intangible assets, or the 4Cs (Human, Customer, Structural and Social) on a regular basis. Most accounting and management systems today do not provide you with any feedback on the ongoing value of the business. Focusing on transferrable value first drives all other positive outcomes including increases in sales and profit. Integrating personal and financial goals and plans with business planning assures that you are prepared for all possible events from a personal, financial and business standpoint (a concept called The Three Legs or Master Planning).

The importance of contingency planning must not be underestimated. Owners must realize that 50% of all exits are not voluntary – not on the owner's terms or timeline – due to at least one of the 5 Ds: Death, Disability, Divorce, Distress, Disagreement.

By focusing on regular and relentless execution of actions to protect, build and harvest business value (which again is likely 80-90% of the owner's net worth), owners position themselves to be able to harvest that wealth in good times or bad.



Despite 96% of the respondents indicating that a transition strategy was important for their future and the future of their business, the survey results clearly show that there is room for improvement. **73% of the survey respondents indicated they had accomplished "no education" on the subject of exit planning**. Owners can start by educating themselves and taking control. Today, there are a vast number of resources available from peer groups, advisors, universities and economic development organizations, and there is literature on the subject (for a full list of reading references visit www.snidervalueindex.com).

Advice to Advisors

The “most trusted advisor” status went to the corporate attorney. We were surprised to see only 14% of the owners naming the CPA as their most trusted advisor. Of all the possible advisors to the owner, the CPA is most likely to have the best insight of all outside advisors into the financials and operations of the business. Going beyond self-imposed boundaries and becoming more consultative with the owner as it relates to managing the value of the business and exit options is an opportunity that would benefit them as well as the business owner.

Surprisingly, only 4% of the owners indicated their wealth advisor as their most trusted advisor. This is noteworthy given that the wealth manager is the one advisor (perhaps also the business attorney) that is with the owner through the entire process, not only leading up to the transition event, but is thereafter charged with managing the owner’s windfall after the exit event. They are also vital in helping the owner select and structure the appropriate exit option. This is another indication of the owner’s misunderstanding of the value provided by the wealth advisor before, during and after the exit event and their lack of education related to all their exit options.

Thank you to our contributors.

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And thank you to the respondents in the Greater Nashville market for their contribution by participating in this study, created to educate and empower middle market owners nationwide.

About the Exit Planning Institute

The Exit Planning Institute (EPI) delivers innovative learning experiences, performance-enhancing resources and strategic tools designed to enhance the exit planning profession. Formed in 2005 to serve the needs of CPAs, financial planners and wealth managers, attorneys, commercial bankers, management consultants, M&A advisors, ESOP and family business advisors, the Exit Planning Institute is considered the standard trendsetter in the field of exit planning across the globe. It is the only organization that offers the Certified Exit Planning Advisor (CEPA) Program and qualifies for continuing educational credits with eleven major professional associations, making it the most widely accepted and endorsed professional exit planning program in the world. For more information, please visit www.exit-planning-instutute.org.

About the Certified Exit Planning Advisor (CEPA) Program

The CEPA Program created in 2007, is the only program of its kind. Developed by nationally recognized experts in the field of exit planning, this 5-day executive MBA style program includes 22 modules taught by a faculty of 13 nationally recognized instructors. The CEPA Program offers professionals an innovative learning experience, performance-enhancing resources, and the strategic tools to help them advance their exit planning practices. The program is held five times a year at state-of-the-art executive education centers including the University of Chicago's Booth School of Business and the University of San Francisco's Graduate School of Management downtown campus.

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