

A graphic featuring a target with three arrows hitting the bullseye. The target is on the left, and the arrows are flying from the right towards it. The background is a light blue and white abstract pattern.

WINNING ON *Wednesday*





IT TAKES A **TEAM**

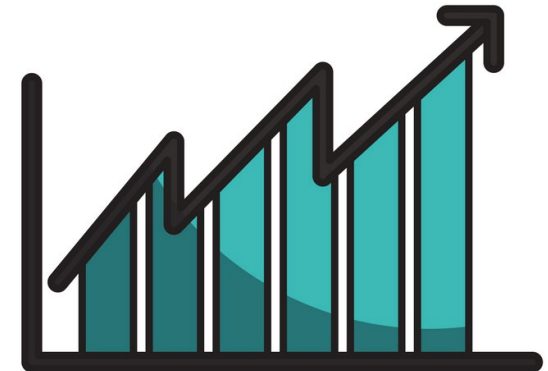
HELPING OUR CLIENTS TRANSFER THEIR BUSINESSES
SUCCESSFULLY & RETIRE IN STYLE



EBITDA – What is it?

Earnings Before Interest Taxes Depreciation & Amortization (EBITDA)

- How do I calculate my EBITDA?
- Are there any other adjustments that need to be made to calculate my businesses EBITDA?
- Why is this an important metric?
- What are some ways that I can increase my EBITDA?



How do I calculate my EBITDA?

EBITDA

- Earnings – Net income (loss) from your business – typically using GAAP or accrual basis financial statements.
- Plus Interest expense
- Plus Income taxes (Mainly applicable for C-Corporations) S-Corporations and Partnerships are pass-through businesses where tax is paid personally and they do not have adjustments for income taxes on the business EBITDA.
- Plus Depreciation & Amortization expense

OR

- $\text{Net Income} + \text{Interest Expense} + \text{Income Taxes} + \text{Depreciation} + \text{Amortization} = \text{EBITDA}$

Are there any other adjustments that need to be made to calculate my businesses EBITDA?

Yes – A buyer wants to know what cash flow they will be getting when purchasing the company. This typically involves adding back owner expenses of the business the buyer will not have. What are some typical add-backs for owners?

- Wages
- Insurance – health, life, disability, etc.
- Retirement Plan – 401k (or SEP/SIMPLE IRA) match + profit sharing
- Payroll taxes
- Vehicle expenses – company owned vehicle for owner
- Rent – owner occupied rent should be adjusted to market value, owner's oftentimes may pay above market value rent to themselves.
- Other personal expenses run through business – travel, phone, etc.

EBITDA Examples

ABC Company, an S-Corporation, has an income statement below. ABC Company has 100,000 of interest expense, 500,000 of depreciation expense and no amortization expense.

Sales	\$10,000,000
Cost of goods sold	<u>- 6,000,000</u>
Profit Margin	4,000,000
Operating Expenses	<u>- 3,000,000</u>
Net income	\$ 1,000,000

EBITDA = \$1,000,000 net income + \$100,000 interest expense + \$500,000 depreciation expense + 0 amortization expense = \$1,600,000. Since the company is an S-Corporation there is no adjustment for income taxes.

EBITDA Examples

Same company - ABC Company has an EBITDA of \$1,600,000. The owner pays themselves a \$250,000 salary and has \$40,000 of benefits paid as well as \$10,000 of personal related items (auto, phone, travel) listed on the financial statements. Company has a reliable management team that can run the company without the owner actively involved.

New EBITDA = \$1,600,000 + \$250,000 + \$40,000 + \$10,000 = \$1,900,000

After considering other expenses the buyer would not incur when purchasing the company, the EBITDA amount increased by \$300,000.

EBITDA Examples

XYZ Corporation, a C-Corporation, has an income statement below. The operating expenses include \$50,000 of interest, \$200,000 of income tax, \$50,000 of depreciation, and \$50,000 of amortization

Sales	\$ 5,000,000
Personnel costs	- 2,500,000
Operating expense	- <u>2,000,000</u>
Net income	\$ 500,000

EBITDA = \$500,000 net income + \$50,000 interest expense + \$200,000 income tax + \$50,000 depreciation expense + \$50,000 amortization expense = \$850,000.

Why is this an important metric?

The most common metric a buyer of a business wants to know is the business EBITDA. This metric informs a buyer what cash flow the company produces on an annual basis.

EBITDA Multiplier – any where from 2.5-10x, typically 3-5x.

Higher EBITDA = Higher multiplier oftentimes

One essential item for succession planning is an effective management team. This can help increase EBITDA.

What are some ways that I can increase my EBITDA?

It depends on your industry, but here are some common methods.

- Increase profit margin
- New customers
- Cross-selling to customers
- Clean financial statements
- Effective procedures within your business
- Find your niche



Coming up next...

5 Keys to Unlocking the Cash in Your Business

February 24th, 2021

Presented by Susan Thomson,
Partner & Licensed Coach, actionCOACH

Identifying Value Gap\$

March 17th, 2021

Presented by Nathan Brinkman, CPWA®
Owner & Founder, Triumph Wealth
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