

P R O S P E R I T A S

EUGEN KLEIN REAL ESTATE BROKERAGE & MARKETING SYSTEMS

OCTOBER 2004: BUSINESS ISSUE

CALCULATING EARNINGS

CORPORATE FINANCE PART I

Editorial



Following last month's issue, I am continuing to showcase many of the new properties and businesses which are coming on, or just recently

on the market. I am calling this issue the "Business issue" – featuring over 20 businesses ranging from \$10,000 to \$1,950,000; everything from franchises to asset sales; all exceptional opportunities for the right purchaser. I have not included some of those larger businesses (Hotels and Liquor Stores) which appeared in last month's "Money" issue.

In keeping with the types of properties featured, this month's article is a continuation of our August issue dealing with purchasing a business in operation. I am taking a closer look at evaluation of business earnings. We are also fortunate to have an article provided us by Bill Humphries and Mark Eikeland of NetFinance.ca on various ways of structuring business financing. This article is fairly long, and will be continued in the November and December Prosperitas issues.

As always, you are welcome to contact me any time with your questions and concerns regarding the disposition of your commercial investments or businesses. ■

Eugen L. Klein
B.Comm (UREC), CRES, ARM®, RI, FRI
eugenklein@shawcable.com



All buyers must use common sense and remember that potential buyers create the market. In order to help with the task of arriving at a good approximation of value, here are six guidelines useful to calculate earnings:

Examine the most recent year's earnings on the seller's latest tax return. It would make sense to look at the last three years, but only to establish a revenue trend; remember as a buyer you are buying the future and not the past. Use these figures to determine projected annual future earnings with you as the new owner. Be aware that such future earnings will depend on your ability as owner; expect that you may have difficulty maintaining the same level of sales over the short term as you gain experience and understand your responsibilities.

Look at the tangible and intangible assets. If there is real estate and inventory included in the sale, your position is theoretically less risky because it is believed that real estate could be sold more easily on the open market and inventory for resale could be more easily liquidated than other business assets. Generally, inventory is

What's In It For Me?

By Eugen Klein, B.Comm(UREC), CRES, ARM®, RI, FRI
Real Estate Broker

valued at cost. Aside from the real estate and inventory for re-sale, other assets should already be included in the multiple-derived business value as they are needed to generate the projected future earnings.

If there is real estate involved but it is not for sale, rental expenses must be subtracted from the earnings figure. The seller did not have to pay rent if he or she owned the property where the business is located, but this would not be the case for you as the buyer. You must take future rent expense into consideration. Conversely if you are buying a business with land, you may wish to structure the transaction so that the ownership of land is under a separate entity from the business. In that

case be sure that if you include the land revenues in the valuation of the land, you subtract them in the valuation based on the earnings of the business. Don't pay for the same thing twice.

Management (owner's) salary, perks, and certain one-time expenses should be added back to the earnings calculation, if these expenses were subtracted from the profit on the tax returns or financial statements. Businesses tend to maximize deductible expenses to minimize taxes. Likewise, depreciation / amortization should be added back to your earnings calculation.

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T E S T I M O N I A L S

"I have encountered few people with the focus and dedication to his clients and to the industry. ...he is also our representative to the National Commercial Council which directs the affairs of commercial realtors at a national level... my assessment of his abilities is shared by realtors throughout the province."

Bruce Sheldon
Vide-Chair, Commercial Division,
Fraser Valley Real Estate Board

"The time and energy that you have taken from your personal life and put into your elected post is a direct benefit to me and my companies and all other realtors and brokers. I just wanted to let you know that your dedication is much appreciated. Thank you for your hard work."

Bob Rennie
Rennie Marketing Systems

"I know that he devotes exactly the same care and attention to his clients' investments as he does to his own. He is a man of tremendous integrity. I encourage you without reservation to rely upon Eugen to answer your real estate needs."

'Rocky' Roy Cameron
BC Lions Alumnus

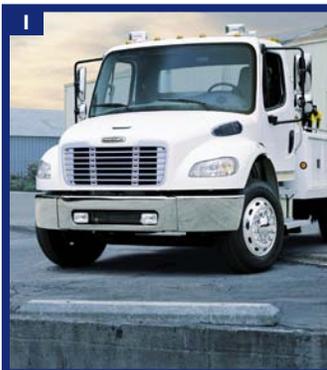
"Eugen is very well qualified... Eugen is a conscientious, hard working member of our profession, and I have every confidence in [him]."

John R. D'Eathe, LL.B., R.I.(B.C.)
Chairman, Penreal Capital Management

Please visit us on the world wide web at www.eugen-klein.com

Goddard & Smith
International Realty Inc.





FEATURED PROPERTY

INTERIOR TRUCKING FIRM

Serves all major Southern BC Highways.
17 Years uninterrupted growth.
13 trucks in fleet.

\$1,950,000



\$600,000



\$599,000



\$525,000



\$399,000



\$250,000



\$195,000



\$195,000



\$190,000



\$150,000

2. INTERNET SOLUTIONS FRANCHISOR

11 full-time employees, 11 existing franchises, \$480,000 revenues, \$49,000 net income, scalable business model, BC/AB/ONT/US expansion ready.

3. YALETOWN RESTAURANT

Well established Yaletown Restaurant. Lot of foot traffic; considerable tenant improvements; all equipment new or in excellent condition.

4. VANCOUVER LANGUAGE SCHOOL

Central Location downtown Vancouver. \$1,300,000 revenues, net income over \$250,000 with manager in place. Expenses down 30%, 3rd straight year of revenue growth.

5. LANGLEY SPORTS BAR/NIGHT CLUB

Established Club with loyal clientele. Minutes from downtown Surrey. 5,000 sq. ft., completed full renovations. Land/bldg also available.

6. FURNITURE MANUFACTURING

First class furniture manufacturing business. Contracts with Pan Pacific and other major hotels. 1 full time and 4 part-time employees. 1750 sq. ft. premises also avail.

7. BURNABY PEDRO'S COFFEE FRANCHISE

Only fair trade organic coffee franchise serving roaster direct coffee. Busy location in Burnaby; after six months averaging \$5.25/sale for 280 sales/day.

8. MAIN ST. PEDRO'S COFFEE FRANCHISE

Only fair trade organic coffee franchise serving roaster direct coffee. Prime location on Main Street, adjacent to Cobb's Bread; huge benefit from shared traffic.

9. TACO TIME NEW WESTMINSTER

Owner retiring, manager in place; offered at below market value. Net cash flow around \$87,000, area is 2,584 sq. ft.

10. SURREY AUTO REPAIR

Mercedes-Benz auto repair and body shop. Exclusive clientele; also licensed car broker 6500 sq. ft.; owner will stay to train.

This communication is not intended to induce a breach of already listed properties or businesses. All information must be verified by the purchaser. Images are representative only.

COMMUNITY

My 'Community' section is dedicated to the extraordinary people who have contributed to my life with exceptional service. I would like to share my good fortune of knowing them with you. Please feel free to convey my recommendation.

BANK OF MONTREAL

Mr. Joe Corrado & Mr. Mark Tower
Vancouver (604) 665-2682

CAPITAL WEST MORTGAGE

Mr. Daymon Eng
Vancouver (604) 899-3799

CHARTERED ACCOUNTANT

Mr. Grant Gilmour
Langley (604) 888-4200

CIBC RESIDENTIAL FINANCE

Mr. Adam Beaudin-Ball
West Vancouver (604) 981-2549

CIBC RESIDENTIAL FINANCE

Mr. Derek Christiansen
Vancouver (604) 220-6161

COMFORT INN

Mrs. Valerie Orr
Vancouver (604) 605-4339

COMMERCIAL MORTGAGES

Mr. Gary Khangura
Vancouver (604) 879-0235

CYPRESS INSPECTIONS LTD.

Mr. Noel Murphy
West Vancouver (604) 312-8606

DIGITAL PRINTING

Mr. Jason Romo
Vancouver (604) 420-3400

FEATURED PROPERTY

TANNING SALON

Tanning salon in central Langley.
1st class equipment; all types of tanning from stand-up to spray-on & hair removal system. 1,500 sq. ft., 3 employees, reasonable rent.

\$160,000



12. DELI / MEAT SHOP

Polish deli and smoked meat manufacturing; retail / wholesale location. Owner will stay and train. Gross rent \$2,190 / month.

13. TACO TIME COQUITLAM

Owner retiring, manager in place; offered at below market value. Net cash flow around \$38,000, area is 1,800 sq. ft..

14. PRINTING SUPPLIES AND MAINTENANCE

Well established supplier and re-manufacturer of printer cartridges. 10 years operation, 2 part time employees, revenues \$196,000.

15. LANGLEY BURGER JOINT

Very popular drive-in, downtown Langley. B liquor license, 52 patio+ 38 indoor seating. Owner will stay to train.

16. TACO TIME LANGLEY

Owner retiring, manager in place; offered at below market value. Net cash flow around \$23,687; area is 2,060 sq. ft.

17. GLOBAL SAFE DISTRIBUTORSHIP

Exclusive distribution rights for revolutionary safety/cleaning product endorsed by major insurers.

18. PHOTOGRAPHY & FRAMING STORE

Five years running; recognized as community's award winning premier framing service. Net income ~ \$45,000.

19. SEAFOOD RESTAURANT

Heart of Walnut Grove; 50 seats & patio. Sales average \$700 per day, open for breakfast, lunch & takeout.

20. GLOBAL SAFE DEALERSHIP

Cleaning & safety product endorsed by top insurers – reduces slip fall claims. Profit \$1 per sq. ft. treated.



\$145,900



\$135,000



\$135,000



\$125,000



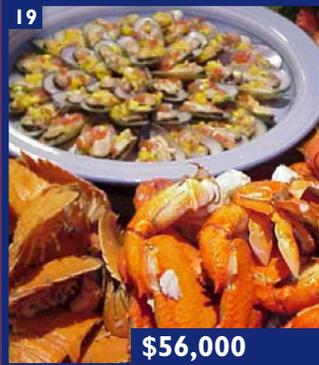
\$115,000



\$107,000



\$99,000



\$56,000



\$10,000

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COMMUNITY

FLOWFORM DESIGN GROUP

Mr. George Verdolaga
Vancouver (604) 321-8008

GRAPHIC DESIGN & ART WORK

Mr. Denis Meyer Jr.
Burnaby (604) 777-0550

MAHOVLICH MARBLE & GRANITE

Mr. Frank Mahovlich
Vancouver (604) 293-0093

MCKITRICK CLARK MCLEOD

Mr. Bruce J. Preston
Vancouver (604) 736-6717

NATIONAL HOME REVIEWS

Mr. Dean Kazoleas
Vancouver (604) 681-2108

PINK LIME SALON & SPA

Mr. Youssef Jawhari
Vancouver (604) 683-7444

PLAN-IT WITH US TRAVEL

Mrs. Pam Gosal
Richmond (604) 916-8044

GRAPHIC DESIGN

Brady Dahmer
Vancouver (604) 737-1637

RENOVATIONS & APPRAISALS

Mr. Chris Lewin North
Vancouver (604) 562-5799

SCOTIA MCLEOD

Mrs. Vanessa Stenner-Campbell
White Rock (604) 535-4749

VANCITY CREDIT UNION

Mr. Joe Chan
Vancouver (604) 877-8296

VANCITY VENTURE CAPITAL

Mr. Axel Christiansen
Vancouver (604) 877-6582

What's In It For Me?



(continued from page 1)

This is a non-cash expense, meaning the owner does not have to pay out of pocket each year.

To summarize:

Earnings = NPBT + OS + FB + D&A

NPBT = Net Profit Before Tax

OS = Owner's Salary

FB = Fringe Benefits

D&A = Depreciation & Amortization

Intangible assets include such things as goodwill, an owner's agreement to not compete, or an owners agreement to provide training or consultation during the transition period. These are accounted for in the value of the business by using a multiple of earnings, even though such assets may well be treated separately at business closing for tax purposes.

Once you have calculated projected annual future earnings, (also known as EBIT, Earnings Before Interest and Taxes) and had your calculations verified by professional accountants, you must consider the risks involved in owning the business. How much you are willing to pay given the risks involved will determine the right earnings multiple. For most businesses somewhere between 3 to 5 times EBIT is reasonable. The multiple is less when there are few tangible assets and more when the business is uniquely attractive.

In summary, the valuation of a business is based on an earnings multiple. The right multiple is, in the eyes of buyers, a matter of assumed risk. Buyers feel better about buying tangible assets that they can appreciate with their five senses – things like real estate and equipment. On the other hand, buyers can also be enticed when there is clearly an attractive opportunity to make money. ■

Corporate Finance I – A Changing Landscape

By Mark Eikeland, CGA
Editor's Note: This is the first in a series of articles on corporate finance.

When Canadian private small business owners need capital their first thought is "the bank." And yet, in many cases, the bank may not be the most appropriate or effective solution or even be interested.

In a recent survey in Profit Magazine, entrepreneurs were asked what they felt were the most serious issues facing Canadian entrepreneurs today. Two issues nearing the top of the list included the lending policies of banks and the scarcity of investment capital. If this is one of the biggest issues facing entrepreneurs, then this is also one of the biggest opportunities to deliver valuable new professional services to entrepreneur clients.

TIMES HAVE CHANGED

Today the bank represents only one funding source out of many. There are more sources of available capital than most entrepreneurs are aware of; yet, at the same time, the plethora of options can be confusing. And this is the primary reason for the difficulty entrepreneurs are having financing their business today. A lack of available capital comes from a lack of information on who the alternative suppliers are, what is available and what their criteria are. This is increasingly a marketplace of specialization and niche lending.

More than ever, the entrepreneur needs to know exactly what his requirements and the lender's preferences are: some lenders look for and do deals that other lenders avoid, these differences exist even among the "big five" major banks. Yesterday, lenders differentiated themselves by focusing on the client relationship - money was mon-



ey. Today, money is a product and lenders differentiate themselves with financing initiatives that focus on target services, industry, region, class, asset type, life cycle/growth stage, product, risk, sales, customer base, growth, leverage, the dollar size of the credit facility, etc.

This is both a good news, bad news story. The good news is that as the lending game continues to open up, more players are entering and the increased competition is bringing added specialization with more competitive and innovative financing options and products to choose from. The bad news is that an already complicated and confusing marketplace becomes even more so.

SHOW ME THE MONEY

Who are these new players, what is their specialization and where do you find them? In British Columbia alone, there are 16 chartered banks, 61 credit unions, 19 factoring companies and 48 foreign banks in operation. Add to this a growing list of U.S. banks such as Wells Fargo, merchant and investment banks, "near-banks" like GE Capital, leasing companies, venture capital companies, asset based lenders, subdebt lenders, boutique lenders, private companies, investment funds, federal and provincial government programs, mortgage and finance companies, enterprise centres, Community Futures Development Corporations, Export Development Corporation and Canadian Commercial Credit

Corporation...

With this new and changing landscape come new trends. As previously mentioned, one such development is that small business financing has become a commodity, a product. Yesterday it was all about the relationship between the entrepreneur and the branch manager. Today the entrepreneur's primary concerns are availability and cost. Yesterday the entrepreneur dealt with a branch manager who, in many cases, funded their request based on the relationship. Today, the branch manager does not have the same decision making powers. Decision making has become centralized and automated outside the branch. We have clients who do not even know their account manager, let alone the branch manager. An entrepreneur will choose a bank or lender relationship based strictly on available credit and cost. And with today's technology, this is a process being done more often remotely through email, fax or the Internet. A good relationship with a warm body is simply secondary and considered a bonus.

Mark Eikeland, CGA, is president and founder of NetFinance.ca, an on-line full service corporate finance resource for accountants and accounting firms throughout BC and Alberta. This area of his practice focuses specifically on corporate finance, and is where clients are assisted in financing their start-up, acquisition, re-organization, and expansion plans. Visit NetFinance.ca for more information. ■

INVESTMENT ■ BUSINESS BROKERAGE ■ SITE SELECTION ■ ASSEMBLY



Eugen L. Klein

B.Comm (UREC), CRES, ARM®, RI, FRI

Broker

Email: eugenklein@shawcable.com
Cell: 604.818.5888
Toll Free: 1.800.818.8599
Direct: 604.691.6622
Fax: 604.691.6688



Michael Mustard

B.Sc(Hons)

Associate Broker

Licensed

Email: mustard@goddard.ca
Direct: 604.691.6660
Fax: 604.691.6688

Please do not hesitate to call me at **604.818.5888**
It is my pleasure to serve your real estate needs.

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