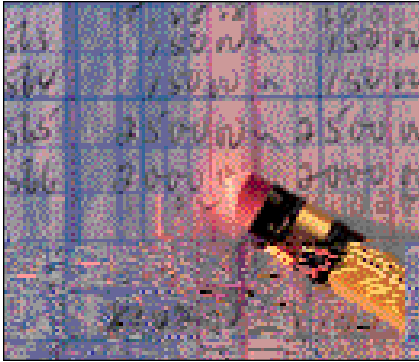


Documenting Your Business Activity Is Essential in Determining Value



Establishing the value of a going business, regardless of its size and market position, always requires significant documentation on the part of the owner(s).

It is difficult, if not impossible, to place an accurate market value on a business and/or convince a prospective buyer of that value without strong documentation to back up the owner's representations. Buyers invariably are guided and counseled by accountants and attorneys, along with others who may be involved in the acquisition process. These advisors are paid to be skeptical, to ask all the "devil's advocate" questions that a buyer might not be thinking about because he or she is enthused about the deal. It is their role to take nothing on faith or by verbal representation; to always ask for the documents and the paperwork proving what a seller is representing to a prospective buyer.

Weak Documentation Hurts

With small, privately held businesses, the available documentation often is not as solid as it should be. Far too often, the financial statements and tax returns are not totally representative of the business' profitability, since many owners are practicing aggressive (though legal) tax avoidance, minimizing profits when possible, and seeking advice from their accounting professionals about limiting year-end tax liability.

The challenge is providing prospective buyers with the required documentation to show the best picture possible

regarding gross margins and expenses applicable to a new owner.

Record Checklist

The following are the records that an owner should have available, for inspection and review by prospective buyers and their advisors:

- Three years' financial statements, with accountant-prepared profit-and-loss (P&L) statements along with federal and state tax returns, including a balance sheet and all schedules. Many buyers also request state sales tax returns, which reflect gross receipts for a certain period.
- If it has been more than 90 days since the close of your last full fiscal/calendar business year, a current P&L will probably be requested. Many owners today are using some sort of internal accounting software (such as Quick Books) to help manage their businesses. These programs, if properly managed, can usually produce a current P&L, though not always with a balance sheet included.
- Bank statements (at least six months' worth of current ones), reflecting receipts and disbursements made through your checking account. If you "park" money in any sort of "sweep" or money market account, also include copies of those statements.
- Check stubs or remittance advices from major third-party payors for a similar period. In today's world of "85 percent + third-party payments," these reports can document your third-party prescription activity and receipts.
- Six to 12 months of prescription department computer printouts reflecting all Rx activity, prescriptions filled, new and refill, generic versus brand, and sorted by third-party payor. I find that, most systems in use today have these reports available to the owner. I also find that some owners are not aware of how to access them and need help in creating the required reports, which can usually be obtained from the help desk at your computer vendor's office. One impor-

tant caveat here is to check how your system reports gross margins and how you have loaded in your cost of goods. I find that the vast majority of these reports DO NOT reflect an accurate gross margin for prescription department activity. In fact, many of them are so skewed, one way or another, that they create skepticism instead of confidence in the buyers' minds. If your system is not providing you with an accurate gross margin for your Rx department, be fully prepared to explain why not and what the accurate number is.

- A copy of your current lease, reflecting all terms, rents, additional charges and assignment restrictions, if any. If you own the building and are planning to lease it to a new owner, then a sheet of paper with your proposed lease terms will suffice.
- A copy of your most recent payroll listing, showing all employees and their compensation, plus a brief job description or title (such as pharmacist, technician, clerk, or bookkeeper).

Armed with these documents, and perhaps a professionally prepared business appraisal or evaluation, owners can enter into any discussion regarding their business' value feeling comfortable about backing up their statements with facts that can and will be accepted by prospective buyers and their advisors. Coming to the table with a fully documented information package in the beginning of these conversations puts you in a solid position to effectively negotiate. If your only goal is to evaluate the business, perhaps for a shareholders' agreement of some kind, it will aid the evaluator in preparing the most accurate documents to support that value. □

TONY DE NICOLA, R.Ph., is president of www.buy-sellapharmacy.com, which is affiliated with NCPA's Independent Pharmacy Matching Service. If you are thinking about buying or selling a pharmacy, call 800-296-IPMS or go to www.ncpanet.org.