FACTORS WHEN VALUING FINANCIAL ADVICE BUSINESSES

PRESENTED BY Queenston Consulting

This White Paper should give you a ball park estimate of the value of a financial advice firm. The vast majority of advisors either want to buy a business or are considering a succession plan. There are many misconceptions in the market place.

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CONSIDER THE FOLLOWING MISCONCEPTIONS

1. Businesses are worth 2.5 - 3 times trails and renewals.

I have seen businesses sell for 1.5x and the buyer paid too much. I have seen businesses sell for 5x. There are many variables to consider before one gets to the “price”.

2. No money up front and paid over 10 years.

The no money down model only works when the advisor is not familiar with what is happening with deals in the market place. Most advisors have a business now not a “book of business” where the revenue is more predictable than the old sales model. Most transactions have 25% to 75% paid up front and the balance paid over 3 to 7 years.

3. There are tons of buyers out there!

There are tons of advisors interested in buying – this is true. There are not a ton of advisors qualified to buy. If the buyer is interested but NOT qualified - they are not a good buyer. Buyers should be selected with a very precise list of qualifications. The converse is also true – not every business for sale is a good fit for every buyer.

4. Sell to the most successful buyer you know.

I see this all the time – seller approaches a buyer who they know will buy their business – the seller just put all the power in the hands of their prospective buyer. Often-times that “successful” buyer is not who you – and many others - think they are.

5. My retirement plan is … sitting on my trails and renewals.

In some ways I understand this concept – it is a lifestyle business model. The problems are:

- it is not fair to your clients;
- it is not fair to your family if you get hit by a bus;
- it is peeing off your Dealer and your MGA; and
- you may be short changing yourself financially.

Do the math – if you have a net income before taxes but after operating expenses - is $200,000 – your business is probably worth $750,000+. This is probably a capital gain and therefore taxed at 0 – 25% vs 50% - PLUS you sign an employment contract or a referral agreement and you will continue to generate more business income. Remember – selling all or part of your business does not mean an exit strategy.

KEY FACTORS THAT IMPACT VALUE AND PRICE

1. Transition Risk

How many clients will stick around if the current owner is not there? There are many variables to consider when evaluating this question. These include, but are not limited to: is the owner sticking around for a few years? Is there a good long term assistant preferably licensed? Is there a clearly defined process for servicing existing clients and converting prospects to clients? Is technology current? CRM up-to-date?

2. Quality of Cash Flow

The key to getting the best price is to know how much of the revenue is repeatable to a new advisor. Business model is very important. Investment management fees vs transaction commissions; annual planning fees; renewals vs FYC; how much repeatable business – PACs; Group Insurance; Term Insurance; are there other advisors in your office sharing overhead (i.e. reducing expenses); etc.

3. Growth prospects

The most important indicator of future growth is the demographics of the current clients. What is the average age; profession; geography; Etc? Average age in 50s and high income earners have more growth prospects than retired clients. The other important factor with demographics is that the business acquiring these clients should already be successful be in that market.

4. Marketability (supply and demand)

Currently we are experiencing a seller's market. Prices are increasing as interest rates stay low, financing is available and the financial markets are buoyant. Those macro factors are very important but so are the micro factors. Platform (MFDA, IIROC, MGA, ICPM, Exempt Market, Referral fee business, etc.), geography, business model, dealer of seller, dealer of buyer, flexibility of buyer and seller – all of these factors will determine the price of the business.

KEY FACTORS THAT IMPACT VALUE AND PRICE (CONT.)

5. The Perfect Buyer

The perfect buyer will pay more because the seller's business is the perfect seller! The right demographics, right business model and the right average household assets mean the buyer should pay more than average. The perfect buyer recognizes that that there are economies of scale – higher payout than seller, reduced expenses on a percentage basis, available capacity in their existing business and the synergy of having a larger presence in their market or a foot hold in another market. This means 25 – 50% more on average. This translates into 100s of thousands dollars for the average business.

Queenston is Canada's premier M&A firm in Canada in the financial advice industry. We have valued and transitioned over $50 million in value and over $3 billion in AUM. We do valuations, assist in negotiating terms of a buy or sell, work with clients in designing a succession plan and work with buyers and sellers seeking that perfect deal.

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