



# APRO FINANCIAL FOCUS

Understanding the Value of Your Business

Presented by: Mike Helton, CPA | January 16, 2025

# Housekeeping

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# Today's Agenda

- **Introductions**
- **Presentation**
- **Questions & Answers**
- **Feedback**



# Today's Facilitator

CHARLES  
SMITHERMAN  
APRO CEO



# Today's Presenter



**MIKE HELTON**  
**ATTORNEY AT LAW**

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# Headlines

- Basic Financial Statement Understanding
- Exit Strategies
- RTO Valuation Methods
- Quality of Earnings
- Accounting - EBITDA, Cash Flow & Budgeting
- Topics of Interest
  - KPI'S
  - Margins

# Basic Financial Statement Understanding

Why do I need financial statements prepared?

- Needs of the client (Fiscal Management or Tax return preparation)
- Needs of creditors
- Needs of investors
- SEC or Government requirements

# Levels of CPA Prepared Financial Statements

- Compiled Financial Statements – Compilation
- Reviewed Financial Statements – Review
- Audited Financial Statements – Audit

# Types of Financial Statements

- Balance Sheet
- Income Statement (P&L)
- Statement of Cash Flows

# Exit Strategies

- Timing
- Reasons to Exit
- Structure
- Financial
- Operational

# Timing

- When you Exit depends on your Reason to Exit
- Patience is a virtue
- Collaboration with advisory team is critical

# Reasons to Exit

- Retirement / Lack of Succession Plan
- Unexpected Health concern / Death
- Economic Uncertainty / Regulatory Changes
- RTO is NOT the right business for you...
- Competitive Threats
- Receive An offer you can't refuse
- Bad location / territory

# Structure

- Sell Assets – Buyer doesn't want your history
  - Who is buying RTO businesses these days?
- Sell / Transfer Stock or LLC interest – Identify potential Successors
  - Sell / Transfer all at once
  - Controlled Succession over time – Sale or Gift
    - Family
    - Key Employees / Partners – Create & Fund Buy-Sell Agreements
    - Outsiders
- Merger
- Liquidation / Bankruptcy



# Financial Matters to Plan Exit

- Valuation / Quality of Earnings
  - Need for Cash Now?
  - Earn Out / Paid Later?
- Seller Finance – who wants to be a bank?
- Bank Restrictions on Change of Control of Enterprise
- Tax Consequences / Allocation of Purchase Price
  - Tangible vs. Intangible Value

# Operational

- POS System must be trustworthy
- Streamlined and efficient business processes
  - Online presence and ability to do business and take payments
- Do you know your own EBITDA / Cash Flow?
- Do you know your own margins?
- Financial Statements must be clean
- Employment policies, benefits and culture must be considered
- Are your location Lease agreements transferable?
- Are your Delivery Truck Leases transferable?

# RTO Valuation Methods

1. Average Recurring Revenue for a period (3, 6, 12 months) X Multiple = On Rent Inventory Value
  - + Value of Fleet (less debt attached)
  - + Value of Fixed Assets
  - + Value of idle inventory (or a % of value)
2. Free Cash Flow X Multiple (I will show you later why I don't say EBITDA)
3. Sentimental Value – Zero x ANY Multiple = ZERO

# RTO Valuations, con't

- Other Factors to consider:
  - Terms of Location Leases in place and Deposits
  - Utility Deposits?
  - Employee Benefits to keep labor force in place
  - A/P Cutoff and Customer Deposits (floating fund) Assumed?
- CPA's Use 3 Common Valuation Approaches: Market, Asset & Income (Discounted Cash Flow) Approach



# The Multiple...

- The “Multiple” is based on risk assessment of future cash flow.
  - A “multiple” is equal to the mathematical *inverse* of the Capitalization (“Cap”) Rate.
  - The Cap rate is the Discount Rate less the long-term expected Growth Rate.

# Discount Rate

- The discount rate is the Rate of Return that investors require. This Rate could incorporate the “build up” of the following risk components:
  - Risk Free Rate – the rate of return available on a risk-free security (i.e., 20-year Treasury Bond yield)
  - Equity Risk Premium – the rate of return to reflect the additional risk of investing in the stock market over the risk-free security (i.e., S&P 500 stocks)
  - Size Premium – the reward for investing in smaller companies
  - Specific company risk premium – the reward for investing in a specific company and industry

# Example...Discount Rate

Risk Free Rate	4.50%
+ Equity Risk Premium	6.50%
+ Size Premium	6.0%
<u>+ Specific Company Risk Premium</u>	<u>7.0%</u>
Discount Rate (or Rate of Return)	24.0%

# The Capitalization Rate

Discount Rate (ROR)	24.0%
<u>Less: Growth Rate</u>	<u>4%</u>
Cap Rate	20%

- As the Cap Rate Grows, Valuation comes Down!
- As the Cap Rate Grows, Investment is Riskier!

# Value Computation Example

Free Cash Flow    \$200,000

Cap Rate                    20%

1. Valuation =  $\$200,000 / .20 = \$1,000,000$
2. Valuation =  $\$200,000 \times 5 = \$1,000,000$

Buyer is willing to give \$1M today for the right to receive \$200K annually for the duration of holding an investment

# Quality of Earnings

- "Quality of earnings" (QofE) refers to the financial due diligence conducted by a buyer during a transaction.
- The process involves analyzing the seller's financial statements, including revenue recognition, cost matching, customer diversity, and operational expenses.
- While QofE is mainly for the buyer, sellers can also benefit from undergoing a similar process before going to market.
- Benefits of seller due diligence includes increased transaction value, reduced risk of price reductions, faster closing process, better market readiness, competitive advantage, and enhanced confidence.



# Quality of Earnings cont'd

- For more information see the related article from our valuation team@  
<https://www.rgcocpa.com/news/selling-your-business-are-your-earnings-quality-earnings-2021/>



# EBITDA & Free Cash Flow

Earnings (Net Income) Before,

+ Interest Expense

+ Taxes (based on income)

+ Depreciation of Fixed Assets (**Not Rental Units**)

+ Amortization

EBITDA

# EBITDA to Free Cash Flow

## EBITDA

- + Cost of Inventory per Books (Charge-offs, EPO, Retail)
- + Rental Unit Depreciation
- Inventory purchased
- Debt Payments (P&I) Required
- Fixed Asset Purchases

## Free Cash Flow



# Cash Flow Planning / Improvement

- It begins with a Budget...
- How do you Budget cash Inflow?
- How do you Budget cash Outflow?

# Cash Inflow Budget

Monthly Rental Revenue (IDEAL, PARR, SMRR, Potential)	\$50,000
x Collection %	88%
<u>x (1 + 22% for Fees) (Excludes Retail Sales)</u>	<u>1.22</u>
Monthly Collections	\$53,680

# Inventory Cost Formula

Monthly Recurring Collections	\$53,680
<u>Cost of Goods %</u>	<u>35%</u>
Inventory Cost Budget	\$18,788
Cash Flow Remaining to fund Overhead	\$34,892

# Inventory Outflow Budget

<b>Metrics</b>	<b>In Units</b>
• Growth	5 Units
• Pay Outs	27 Units
• Charge Offs	8 Units
• Retail Sales	<u>2 Units</u>
• Total Units Needed	<b>44 Units</b>
• ACU	\$427
• Inventory Budget	\$18,788



# Breakeven fixed cost calculator

• Increase in Overhead per Month	\$ 5,000
• Divided by Gross Margin (100% – COGS %)	65%
• Monthly Recurring Revenue Needed	\$ 7,692
• Divided by Avg. Potential / Unit	<u>\$ 80</u>
• Number of Units Required	97
• X Avg. Cost / Unit	<u>\$ 427</u>
Investment in new Revenue Stream to cover new cost	\$ 41,420

*Could use the Unit model with Customers and Agreements*



# Other Common KPI's

- Units, Agreements, Customer Count +/-
  - Balance On Rent – BOR (Units, Agreements, Customers)
- Avg. Potential (Revenue)/(Units, Agreements, Customers)
- Avg. Cost /(Units, Agreements, Customers)
- Deliveries / Pickups
- Keep Rate
- Delinquency
- Collection % of Potential Revenue
- Cost of Goods % / Gross Margin
- Cost Recovery Length

# Benchmark Margins

- Some common P&L Benchmarks
  - Cost of sales                      35% of Gross Revenue
  - Turn Length                        Contract Length x 35%
    - (24 Mos Contract = 8.4 Mos)
  - Personnel                            25% of Revenue
  - Occupancy                            10% of Revenue
  - Delivery                                5% of Revenue
  - Selling / Marketing                6% of Revenue
  - Other G&A =                         8% of Revenue
  
- 4 Wall Profit =                        11% of Revenue
  - *For Discussion only. Compare to your actual metrics.*

Thank You!

Questions/Discussion



# APRO's Next Webinar

## New Year, New Commitment to Using AI

Presented By:  
Lori Gracey  
February 20, 2025

**NEW YEAR,  
NEW  
COMMITMENT  
TO USING AI**

AN @PRO™ WEBINAR



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4. Are there any areas from today's webinar that you'd like to explore further?

(Please describe in the chat.)



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