



# **Self-Directed Retirement Plans & Investing in a Privately Held Business**

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&  
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# Security Trust Company

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## Self-Directed Retirement Accounts

### ● What is a Self-directed Account?

- You may choose any allowable type of asset
  - Includes non-traditional assets like real estate
  - Offers you true diversification
  
- You manage your retirement plan investments
  
- You have control

# Types of Retirement Plans

- **Traditional IRA**
- **Roth IRA**
- **SEP/SARSEP/SIMPLE**
- **401 k – prior employer**
- **403 b – prior employer**
- **TSA – prior employer**
- **TSP – prior employer**
- **Keogh**
- **Solo 401(k)**
- **401(k) plans**



# Some Investment Options

- **Single/Multi-family homes**
- **Vacation investment property**
- **Tax Liens**
- **Raw Land/Building Lots**
- **Commercial Buildings**
- **Real Estate Syndications**
- **Mortgages/Loans**
- **Private Business Investments**
- **Operating Businesses**
- **Foreign Currency/Options/Futures**
- **Stocks/Bonds/Mutual Funds**

# Guidelines for Self-Directing

- **Administrative requirements**
  - Annual valuation of plan
  - Annual report to IRS (5498)
  - Books and records
  - State filings
  - Tax returns



# Guidelines for Self-Directing

## **Prohibited Assets:**

- **Life Insurance Contracts (except Solo 401(k))**
- **Collectibles (i.e. rugs, works of art, stamps, coins)**

## **Prohibited transactions:**

- **Transactions not for the exclusive benefit of the account**
- **Can't borrow from Retirement Account**
- **Can't pledge Retirement Account assets to secure loan**
- **Can't utilize credit or guarantee to obtain loan for account**
- **Can't benefit any disqualified person**



# Guidelines for Self-Directing

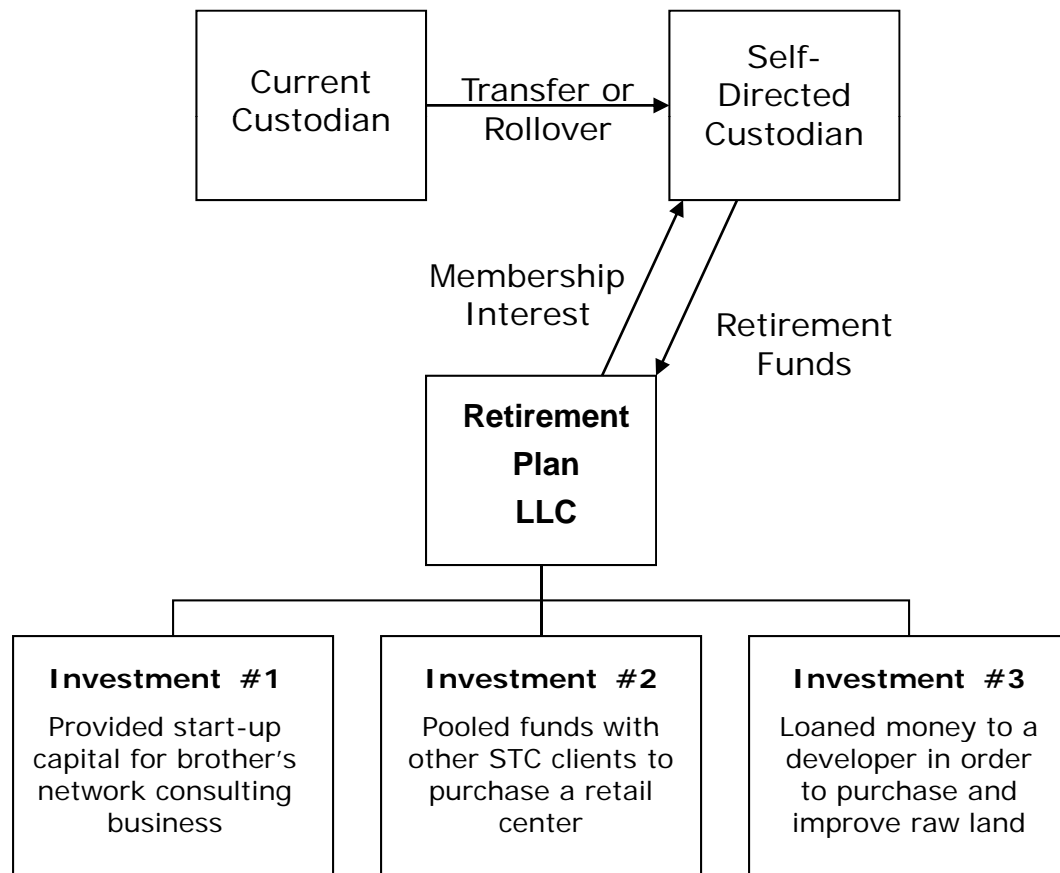
## Disqualified persons:

- “You”
- **Certain family members**
  - Ascendants
  - Descendants
  - Lateral family members are not disqualified
- **Company if you are a majority shareholder**
- **Company if you are officer, director, HCE**

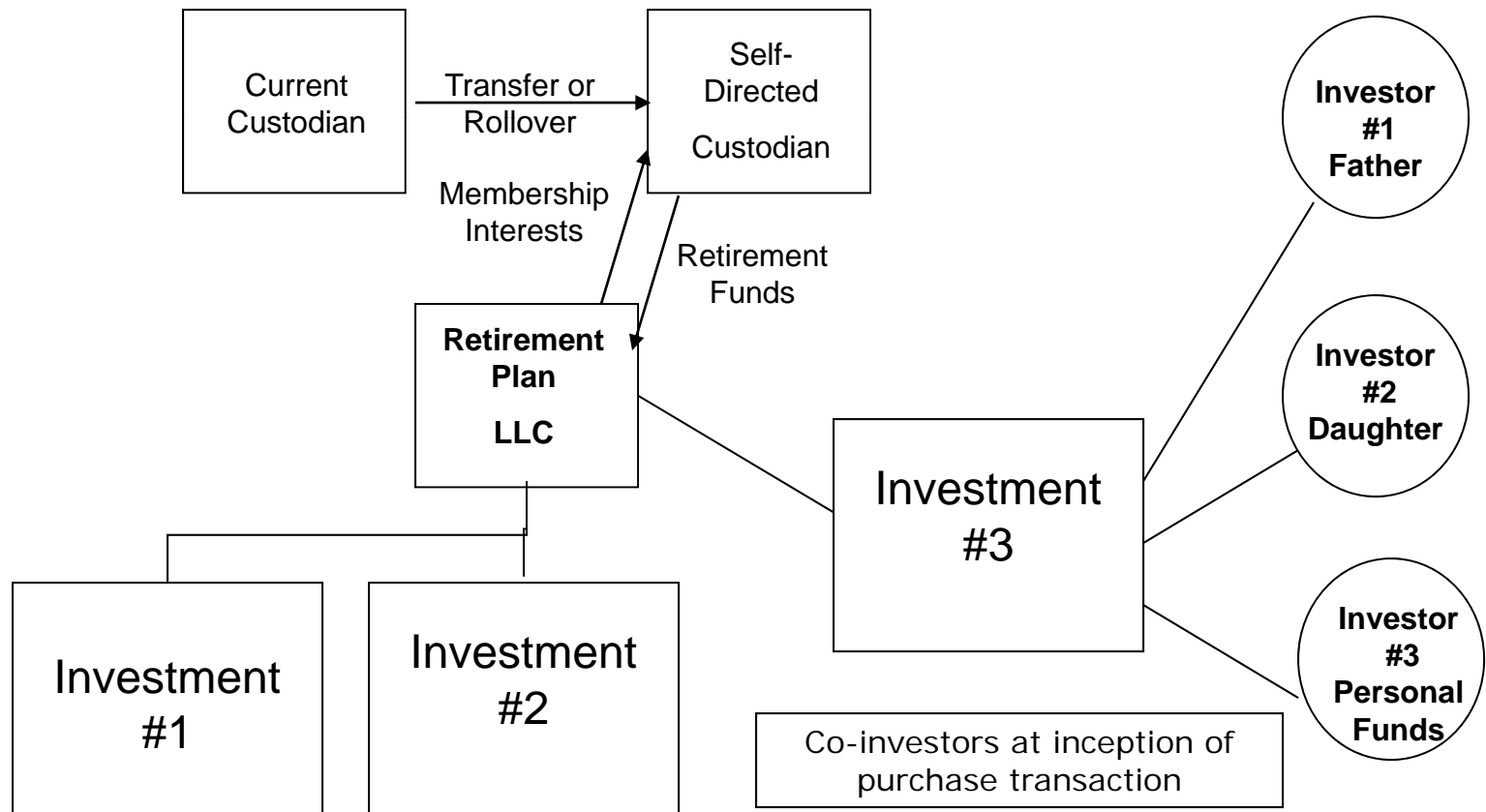
## Benefits of the LLC Structure

- **Offers maximum flexibility**
- **Provides additional asset protection**
- **‘Checkbook control’ over retirement funds**
  - **Immediate response to investment opportunities**
- **Simplifies asset titling**
- **Ease of pooling**

# IRA LLC Structure



# Retirement Plan LLC Structure



## Security Trust's Full-Service Approach

- Retirement Plan LLC structure setup
- Protected 'checkbook control'
- CPAs & attorneys to answer technical questions
- Guidance on transaction compliance
- Handle all the 'back office' support
- Maintain LLC financial statements
- Supervise regulatory reporting
- Oversee annual valuation

# Investing in a Privately Held Business

**Jim Eshleman, Principal  
Strategic Endeavors LLC**

**Specializing in ownership  
transfer planning and execution  
for privately held businesses.**

## Disclaimer

- Strategic Endeavors LLC is a business brokerage firm representing either buyers or sellers of privately held businesses in asset sale transactions (as opposed to stock sale transactions).
- Strategic Endeavors LLC is not a registered investment advisor and does not engage in the sale of securities, capital raising, and other activities regulated by the SEC or state securities authorities.
- Strategic Endeavors LLC is not qualified to provide legal or tax advice and always encourages participants in transactions to consult with attorneys, accountants, and other professional advisors when engaging in the business acquisition process.

## Why Buy a Business?

- You may have knowledge and expertise in small business operations and want to passively own a business that is locally controlled.
- You may know a non-disqualified party that you would like to fund to operate a small business that you would own.
- You may be seeking a higher return than is available on other types of investments.



## Risk vs. Reward

- Guaranteed (CD) 1 to 3%
- Bonds – Municipal or Corporate 3 to 8%
- Index Fund – broad diversification 5 to 10%
- Mutual Fund – targeted segments 8 to 12%
- Large Cap Stock 12 to 18%
- Small Privately Held Co. 25 to 35%

# Terminology

## Main Street Business

Sale price < \$1 mil

Owner operated (Mom & Pop)

SDE (Seller's Discretionary Earnings) - Cash Flow

## Middle Market Business

Sale Price > \$1 mil

Owner or Professional Mgt. operated

EBITDA (Earnings bef. Int., Tax, Deprec.& Amort.) –  
Cash Flow

## So What is Cash Flow?

Profit/(Loss) of Business  
Compensation of 1 Owner  
Interest  
Deprec./Amort.  
Other Adjustments

**SDE Cash Flow**

Less Market Replacement Comp. for Mgr.

**EBITDA Cash Flow**

# Typical Small Business Pricing

Main Street Businesses

Sell for 1 to 4 X SDE

Middle Market Businesses

Sell for 4 to 6 X EBITDA

Above are typical ranges and are asset sale prices. Ultimately a business is worth what a buyer is willing to pay.

## What's included in the Price?

### Included:

- ✓ Furn., fixtures & equip.
- ✓ Market rate lease.
- ✓ Goodwill and intangible assets.

### Excluded:

- ✓ Cash & cash equiv.
- ✓ Accounts receivable.
- ✓ Prepaid expenses.
- ✓ Real estate.
- ✓ Non-operating assets.
- ✓ Liabilities.

Open to debate – amount of inventory included.

# How Do You Find Opportunities?

1. Business Listing Websites
2. Contact business brokers in your area.
3. Business opportunity section in classifieds in local newspaper.
4. Attorneys and accountants may know of Owners that want to sell.
5. Ask a business owner directly.
6. Post a wanted to buy ad in the classifieds.
7. Check classifieds on trade associations, magazines, etc.
8. Hire a business broker to search.

# Business Listing Websites

[www.bizbuysell.com](http://www.bizbuysell.com)

[www.bizquest.com](http://www.bizquest.com)

[www.businessbroker.net](http://www.businessbroker.net)

[www.sellbiztoday.com](http://www.sellbiztoday.com)

[www.bizilla.com](http://www.bizilla.com)

[www.pennbba.com](http://www.pennbba.com)

## Business Listing Websites

- Can search by state
- Can search by county
- Can search by type of business
- Can search by price of business
- Can search by keyword



# Process Overview

- Contact broker or seller
- Complete non-disclosure agreement and screening information
- Receive information describing the business
- Engage in back and forth dialogue and questions about the business
- Have site visit to see the business and meet the seller
- Make an offer
- Negotiation and offer acceptance
- Financing sought and confirmed
- Due diligence investigation
- Legal documentation
- Closing

## Qualitative evaluation of the business?

Business presentations typically show 3 to 5 years of financial history.

Some basic questions to ask:

1. Why is the business for sale?
2. Explain the trends in the business financials?
3. What are the business's competitive advantages?
4. How would you grow this business?
5. What are the weaknesses and how could the business be improved?
6. Where is the product in its life cycle?
7. How many customers are there and is any customer more than 10% of sales?

## Qualitative evaluation of the business (Continued)?

8. What is the seller's role in the business? Probe for personal relationships that may not be able to be duplicated.
9. Who are key employees, what do they do, what do they know, and is it likely they will stay?
10. What capital assets are used in the business, are they up to date, and what are replacement plans for the future?
11. How much working capital is required to run the business?
12. Does the business have a line of credit and how is it used?
13. Who are the trade associations for the industry?
14. More probing in all of the key areas: sales, operations and finance

## Quantitative evaluation of business?

Justification to Purchase Test

SDE Cash Flow

less Mgt. Replacement Comp.

less Debt Service (if leveraged)

less Capital Expenditures

Pre-tax Return/Add'l Investment

## Case # 1 – All Cash Deal

### Target Co.

Sales	\$ 350,000
Profit (after all expenses)	\$ 35,000
Owner Salary	\$ 80,000
Deprec.	\$ 5,000
Interest	\$ 2,500

## Case # 1 – All Cash Deal

SDE Cash Flow

= Profit + Owner Comp + Deprec. + Interest

= \$ 122,500

Cash Price for business - Say \$290,000

Price as a multiple of SDE = 2.37

## Case # 1 – All Cash Deal

### Justification To Purchase Test

SDE Cash Flow	\$ 122,500
less Mgr Salary	\$ (50,000)
less Debt Service	\$ 0
<u>less Capital Expenditures</u>	<u>\$ (5,000)</u>
Pre-tax Return	\$ 67,500

$$\text{ROI} = \$67,500 / \$290,000 = 23.3\%$$

## Case # 1 – All Cash Deal

Initial Investment	\$ 290,000
5 Annual Returns	
5 X \$67,500	\$ 337,500
Sell @ end of Yr 5	\$ 290,000
Total Cash Returned	\$ 627,500
Equivalent ROI	16.7%



## Case # 2 – Leveraged Deal

### Target Co.

Sales	\$ 350,000
Profit (after all expenses)	\$ 35,000
Owner Salary	\$ 80,000
Deprec.	\$ 5,000
Interest	\$ 2,500

## Case # 2 – Leveraged Deal

SDE Cash Flow still is \$122,500.

Assume Seller Financing at 33% down and 67% financed for 5 yrs at 8% interest.

To finance, Seller demands a 15% premium in the Price =  $1.15 \times \$290,000 = \$333,500$ .

Leveraged sale multiple of SDE = 2.72.

Cash Down Payment = \$110,055

Seller Note = \$223,445 at 8% interest.

Annual P&I = \$54,368

## Case # 2 – Leveraged Deal

### Justification To Purchase Test

SDE Cash Flow	\$ 122,500
less Mgr Salary	\$ (50,000)
less Debt Service	\$ (54,368)
<u>less Capital Expenditures</u>	<u>\$ (5,000)</u>
Pre-tax Return	\$ 13,132

## Case # 2 – Leveraged Deal

Initial Investment	\$ 110,055
5 Annual Returns	
5 X \$13,132	\$ 65,660
Sell @ end of Yr 5	\$ 290,000
Total Cash Returned	\$ 355,660
Equivalent ROI	26.4%

## Closing Thoughts on Buying a Business in Your Self-directed IRA

- When buying a business you are purchasing the future stream of free cash flows the business will generate. How secure is the future for the business you are buying?
- If you can grow the business, you may be able to increase the value of your investment in addition to annual returns (i.e. \$2.5 of value for every add'l \$1 of cash flow).

## Closing Thoughts on Buying a Business in Your Self-directed IRA

- Leverage will enable you to increase the return if there is a way to finance the purchase (i.e. seller financing?).
- Be careful that your plans with respect to ownership and operation do not compromise the compliance of your retirement plan.
- Seek competent counsel on tax consequences on annual business income and appreciation that may occur when exiting the business.

**For questions and assistance with  
buying or selling a business contact:**

**Jim Eshleman**

**Certified Business Intermediary  
Strategic Endeavors LLC**

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## How can Security Trust serve you?

### Do you...

- want to open a self-directed retirement account now?
- have clients or colleagues who would be interested in self-direction?
- need more information?



# Security Trust Company

- **Contact your STC representative.**
- **Website: [www.securitytrustcompany.com](http://www.securitytrustcompany.com)**
- **Corporate: 1-866-682-3683**