

# HOW TO CALCULATE SDE

Seller's Discretionary Earnings in 3 easy steps.

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Sell Your Business 101 #VRVALUE

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## About Seller's Discretionary Earnings (SDE)



If interested parties are individual buyers who will become owner-operators, it is important to calculate the full economic benefit to the new owner, using SDE.

This figure includes all owner compensation and benefits as is, someone buying a job is seeking a lifestyle and interested in how much money they can personally make. In transactions where value is based on a multiple of SDE, the deal structure is generally an asset sale where tangible and intangible assets of the business are sold. An asset sale sometimes includes inventory of the business, but does not include the cash, accounts receivable nor any short or long term liabilities of the business.



SDE is most commonly used for company earnings less than or equal to \$1,000,000, where buyers are individuals.

## 3 Years Tax Returns

01

Pull out your tax returns for the years you'd like to calculate SDE, using the last three years is common. Perform the steps below for each tax year as each will have its own SDE.



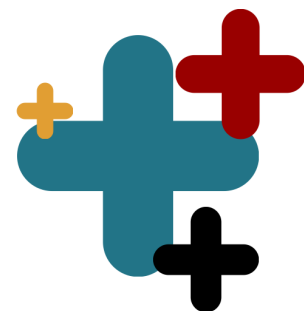
## Add up these numbers

02

Generally, you can find these numbers on the first page of your tax returns:

Find ordinary business income (pre-tax earnings)

- + Add Interest Expense
- + Add Depreciation Expense
- + Add Amortization Expense  
(this may be listed in the itemized expense statement further back in the tax return)
- + Add owner compensation and benefits. Do NOT normalize to align with the market.



We are using ordinary business income from tax returns, so taxes haven't been deducted and therefore do not need to be added back.

## Adjust for unusual expenses

03

Now that you've found SDE in Step 2, review your expenses for the period you've completed the calculation for. Were there one-time and non-recurring expenses? Identify any unusual expenses you don't see year to year and add them back. Charitable donations, excessive travel and entertainment expenses, one-time bad debt write-offs, etc.



Although it is best to work with a professional to determine the business sale price or listing price range, an owner can use estimated SDE and an appropriate multiple of 1-3 times to get an idea of the company's value.

## VR BUSINESS SALES | MERGERS & ACQUISITIONS

### COMPANY OVERVIEW

VR Business Sales New Haven represents owners of businesses valued between \$500,000 and \$25 million or with annual revenues from \$1 million to \$30 million. The office provides exceptional merger and acquisition advisory services to companies operating within a wide range of industry segments in Connecticut, Southern New England and Metro NY. Independently owned and operated, the office consistently ranks within the Top 10 of over 50 offices worldwide with the VR franchise network.

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