

# The SDE Recasting Cheat Sheet

How to Find the Real Profit in Any Business — and Use It to Negotiate

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**Sellers don't hide profit on purpose. They've just spent years running personal expenses through the business. Your job is to find them.**

SDE stands for Seller's Discretionary Earnings — the total financial benefit an owner receives from a business in a given year. It is the most important number in small business valuation, and it almost never matches what shows up on the P&L;

Recasting is the process of adding back legitimate owner expenses to arrive at the true SDE. This is standard practice. Every serious buyer and broker does it. If you don't do it, you will underpay for cash flow — or overpay for a business that looks profitable but isn't.

## Step 1: Start with Net Income

Pull the business's net income from the most recent full-year tax return (or CPA-prepared P&L;). This is your starting point.

## Step 2: Add Back Owner Compensation

The owner's salary runs through the books as an expense. But in an acquisition, you're replacing the owner — so their salary is not a true cost of running the business. Add it back.

- Owner salary
- Owner payroll taxes
- Owner bonuses

## Step 3: Add Back Personal Expenses Run Through the Business

This is where the real money hides. Owners legally run personal expenses through the business. Common add-backs include:

- Personal vehicle (lease payments, insurance, fuel)
- Personal cell phones
- Personal travel and meals (family trips, non-business dining)

- Life insurance premiums for the owner
- Health insurance for owner and family
- Home office deductions
- Personal subscriptions and memberships
- Depreciation (non-cash expense — add back)
- One-time legal or accounting fees (non-recurring)
- One-time repairs or capital expenditures

### Live Example: ABC Landscaping

LINE ITEM	AMOUNT
Net Income (from tax return)	\$142,000
+ Owner salary	\$85,000
+ Owner payroll taxes	\$6,500
+ Owner health insurance	\$18,000
+ Personal vehicle (truck)	\$14,400
+ Personal cell phone	\$2,400
+ Depreciation (non-cash)	\$22,000
+ One-time legal fee (non-recurring)	\$8,500
<b>= Recast SDE</b>	<b>\$298,800</b>

At a 3x SDE multiple, this business isn't worth \$426,000 (3x net income). It's worth **\$896,400** — or the buyer could negotiate using recast SDE as leverage to reframe the entire deal.

### Using SDE in Negotiation

If a seller is asking 3.5x net income (\$497,000), you can counter:

- 'Your recast SDE is \$298,800. At 3x recast SDE, fair value is \$896,400 — but we need to verify these add-backs. Let us run due diligence and we'll honor a fair multiple of verified SDE.'

This shifts the conversation from price to proof — and puts you in the driver's seat.

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