

Stop Lights in the Fast Lane

A primer for the entrepreneur/business owner when considering the sale of their business.

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Selling a business is not a trivial task. Many speed bumps can be eliminated or minimized with some attention and advanced planning. At all costs, you should avoid waiting for the closing table to learn that your business had some "issues" that will disinterest the buyer, reduce multiples or increase discounts and adjustments.

In the sections below, you will find a collection of items to address to ensure that green lights are glowing through the finish line. Arguably, each section merits an entire chapter in a book, however, for the busy executive; here are some of the highlights:

Start Early

This first step can't be overemphasized. Schedule time on your calendar each day/week to get all of your ducks in a row.

Shareholder Consensus

Review the internal shareholder environment. Make sure that all of the owners agree that the sale of your company is the correct liquidity event given your current business situation, strategic plan and other business dynamics. Schedule an internal meeting to get all stakeholder input on a potential sale. Take official notes, for some may develop selective amnesia, as the potential sale progresses. Do you have any minority groups or individuals that might resist the liquidity event? Do you have an ex-partner that might want a piece of the action? Do you have a current/former shareholder that has been through a divorce, potentially creating an expectation that he/she owns a stake in the business? Are there any owner siblings involved in the business? Children disputes will most likely foul the deal for potential buyers, and future managers could spend a ton of energy and corporate resources cleaning up the mess and/or acquired corporate culture.

Maintain Focus on the Current Business

Don't take your eye off the ball. Since most entrepreneurs/business leaders can successfully manage the sale of a business, their natural reaction is to take on the project as an additional task to their already growing list of daily responsibilities. Don't do it! During the six-to-nine month lead time of the sale, your business valuation can deteriorate. Hire a Business Broker (BB)/Investment Banker (IB) to handle the initial valuation, marketing and day-to-day sales process. The best thing that you can do to help with the final sale price of your firm is to keep focused on growing the business.

Human Resources

Employment related issues such as unfunded pensions and former employee obligations/severance issues can impede deal momentum. Verify that Employee Stock Option/Ownership Plans and Shareholder Agreements align with your desire to sell. Review your insurance policies. Do you have key-man insurance?

Facilities

Environmental issues such as a leaky fuel tank, chipped paint, unsafe facilities, contamination, etc., are all items that can slow or halt a deal. As seen in the residential real estate market, a fresh coat of paint and some fresh flowers in the reception area can improve the potential buyers "feel good" factor when evaluating the business.

Production/Manufacturing

Product warranty related liabilities that may impede future performance.

Taxation

Talk to your tax advisor about any upcoming tax issues that might adversely affect the sale and his/her deal structure preferences to maximize shareholder value. Ensure that the firm is current on all federal, state(s), local, payroll, sales and income tax liabilities.

Finance

Talk to your CFO. Are your loans assumable? Are your financial statements audited? If not, the potential buyers will hire a CPA firm to audit your books, which will likely reduce your valuation. Have a complete set of updated and audited financials available at all times.

Legal

Talk to your corporate counsel regarding past items that might come out of the closet during a buyers Due Diligence (DD) process and deal structures that will best satisfy your shareholders. Ask him/her for a review of all contracts (vendor, customer and strategic relationships), or anyone else in your end-to-end supply chain. Do you have any transferability or assignability issues? Is your Intellectual Property, such as copyrights, trademarks, service marks, patents and ideas, protected? Do you have any Union-related issues that need to be addressed? Are there any "poison pill" clauses in your shareholder agreement or corporate by-laws that can kill the deal?

Sales

Talk to your sales leadership. (If you are the CEO as well as the VP of Sales, talk to yourself, but not in public.) Review current contracts. Cleanup your sales pipeline list. Create a red (lost deal), yellow (major issues exist), green (sales process tracking well) report and make adjustments as needed. Weigh each potential deal and calculate the probability-adjusted pipeline which will be used later in the valuation process. Be conservative, for if your deal closes with an earn-out, you will likely get paid on the performance of closing the opportunities in your pipeline.

Customers

Call your customers proactively to ensure that all is well. Some DD teams may discretely contact clients. Have your internal team develop a red/yellow/green action plan for each client to convert any reds and yellows to greens. Having too many cautionary (yellow) or negative (red) client references may spook the buyer or cause downward pressure on the sale price.

Valuation

Have your BB/IB create a valuation using comps, an in-depth evaluation of the business fundamentals, market conditions, strategic positioning (items covered in my next article). Make sure that your board agrees with the valuation. Ultimately, the market (disguised by one or more serious buyers) will determine the real market value of your business at that particular moment in time. Nothing more, nothing less! Of course there is the rare emotional buyer that is willing to pay

way over market price for a multitude of strategic or personal reasons. The buyer will need to consult their CPAs on how to best handle the excess goodwill (overpayment). Many buyers want to pay a multiple of recent results, such as revenue or EBITDA. On the other hand, sellers want to receive an amount based on future potential, using some variation of a discounted cash flow model. Ultimately, the negotiations team will meet at a price that is perceived as comfortable for both sides of the table.

The Inner Circle

Decide who needs to know about the possible sale. Given the culture and other group dynamics, one might choose to include the entire company in the decision. Some leaders choose to include the customers in the final deal process. Other owners choose to keep the entire process under wraps and disguise the BB/IB teams and possible buyers performing DD as "consultants" or "auditors." Most leaders include a handful of strategic team leaders in the process and do not share any details with the rest of the company or customer until a deal has been reached. Some teams create a code name for the "project" to be used on email, calendars, etc.

Strategic Plan

Is your strategic or business plan up-to-date? Do you have an Executive Summary worthy of handing to a serious High Net Worth investor or corporate buyer? If not, your BB/IB will create this document for you. Have you thought through an integration strategy for each potential buyer. A local acquisition may require closing one office and consolidating teams. A foreign or out-of-state acquisition may require your operations to maintain, if not grow, the buyers regional/international presence.

Health

Review the health and professionalism of the owners. Will the buyers want to acquire your management team? If the tables were turned, would you hire yourself? Given the outcome of your review, have a plan in mind because the buyer may ask about career/succession planning.

Competition

Review your competition. Can the competition throw you a curve ball to derail the deal? If so, what kind? Engage your inner circle team in a contingency planning discussion to perfect your competitive strategy.

What's Your Exit Strategy?

Review your own intentions. What are your motivations? Do you want to cash out and retire or do you want a leadership role in the acquiring firm with an "earn out" over time? Are you looking for a stay package? Some buyers may not give you an option. Think through your plans for each path.

Team Negotiations

Review your acquisition team. Do you have an experienced M&A lawyer, tax lawyer, accountant, etc.? Who will be the lead negotiator? If you intend to maintain a working relationship with the buyer, remove yourself from the point position and let the lawyer or BB/IB take the lead. Most business owners are emotionally connected to the firm, which clouds their ability to successfully negotiate.

Buyer Targeting

Create a target list of perfect buyers (green), unknown buyers (yellow), and nightmare buyers (red). Are you targeting a horizontal buyer that would benefit from a new product/industry offering, or, should you target a vertical buyer that can use your product/service to augment their existing portfolio in the same industry segment? Have weekly team meetings to review progress of each buyer opportunity and reclassify as needed. Update your selling strategy as new market information unfolds.

Are You Ready?

Lastly, your BB/IB will need you to be responsive to prospective buyer requests. Are you committed to this liquidity journey or are you simply

just trying to gauge a retirement planning scenario? If the latter is true, hire a CPA firm to appraise the business value. If your committed to the sale, hire a BB/IB, jump in, be responsive and don't look back.

Good luck. I hope to see you in the "Fast Lane."