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HOW TO SELL YOUR BUSINESS

WHEN TO SELL

The first step in selling a business involves determining not how much or to whom, but *when*. Proper timing can increase the value of your business by millions of dollars. It also has an impact on the quantity and quality of potential buyers, and it affects the company's ability to continue on after you sell.

Ideally, you will have a written exit plan in place that addresses these issues in detail. If not, suggests Currie, start by asking the following kinds of questions:

- When is the right time to sell?
- Do I want to stay with my business after I sell?
- To whom should I sell?
- What is my business really worth?
- What kind of help do I need?
- What are the risks involved in selling?
- What should I be doing now to prepare for the sale?

Of these, the last question may be the most important. Selling a business isn't like selling a car or even a home, where a little bit of paint or some new flowers in the garden can make things look like new. Depending on how you've managed the business, it can take months or even years to get it in presentable shape.

PREPARING FOR THE SALE

Smart business owners begin preparing the business for sale long before they actually put it on the market. Currie offers the following checklist to guide your preparations:

- **Document your vision.** Create a written five-year strategy to help potential buyers see where the company is headed.
- **Prepare audited and reviewed financial statements.** Serious buyers will demand an objective, third-party accounting of your company's financial performance.
- **Make cosmetic improvements.** Like a new coat of paint on a used car, cosmetic improvements don't cost that much and can greatly enhance the appearance of your business.
- **Identify business opportunities.** Create a top 10 list of potential opportunities and have it available for potential buyers.

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- **Recast your financial statements.** Identify non-essential expenses, including excess pay or perks you take out of the business.
- **Perform environmental reviews.** You can't do a deal when faced with unresolved environmental problems.
- **Purge obsolete assets.** Get any non-performing asset off the balance sheet.
- **Settle any existing lawsuits.** With the exception of environmental issues, nothing can stall a deal quicker than the threat of pending litigation.
- **Document operational procedures.** Buyers don't like to think all the secrets are locked inside your head.
- **Evaluate management.** Buyers will always pay more for companies with solid management teams.

DOING THE DEAL

Currie breaks down the process of selling a business into four distinct phases – preparation, marketing, negotiating and closing. Each phase has distinct activities that must be accomplished before moving on to the next phase. The transaction typically takes six months to one year to complete.

Note: This model assumes you have already identified an intermediary to assist in the process of selling your business.

Phase 1: Preparation

Assess the current state of the business and identify any immediate "value enhancers" – tangible or intangible qualities or components that might entice potential buyers to pay a premium. Next, prepare a sale memorandum, also called an "offering" memorandum, which typically includes the following:

- An industry overview, including market growth potential
- A history of the company
- Very basic information about products, customers, employees and competitors
- Future growth opportunities
- Recast income statements

"The offering memorandum is a confidential document privy only to the seller and anyone he or she approves," explains Currie. "It is carefully crafted to provide adequate information to a buyer and elicit a letter of intent, yet restrictive enough to avoid compromising on information that could be harmful to the business."

The next step in this phase involves identifying and qualifying potential buyers. At this point in the proceedings, the more qualified buyers, the better. When investigating potential buyers, ask:

- Does the buyer have the financial resources to complete the deal? Who does the buyer bank with and where is the money coming from? Check all references thoroughly.

- Who approves the deal? How many levels of approval are needed to make the deal and what is their process for buying a company? A lot of people can say "no" to a deal. Make sure you negotiate with the person(s) who can say "yes."
- Does the buyer have a track record of successful acquisitions? Research every deal they have done within the past five to 10 years. Find out how long each deal took to close and how it turned out for all involved.
- Does the buyer have any bankruptcies or pending litigation?
- What is the buyer's motivation? Why do they want to buy your business? Know how you can benefit each type of buyer.

"Don't skimp on your due diligence of prospective buyers," advises Currie. "You never know what piece of information might make or break the deal. It's impossible to know too much about potential buyers."

As the final step in the preparation phase, craft a marketing letter to attract a buyer's interest. This letter must not identify you; however, it must have enough compelling information to elicit a response.

Phase 2: Marketing

Your intermediary will release the marketing letter, followed in a week by telephone contact. If you have a good letter, your intermediary should begin receiving responses within a short period of time. They will respond to interested parties in the following manner:

- Have each prospective buyer sign a confidentiality agreement.
- Begin the process of pre-qualifying the prospects.
- Release the offering memorandum to all qualified buyers.
- Respond to their initial round of questions.
- Prepare additional information as needed.

The next step typically involves a series of off-site meetings where you scrutinize potential buyers before deciding whether or not to let them inside your business. If you decide to proceed, arrange a company visit, preferably at a time when employees are not present.

"We recommend bringing in prospective buyers under the guise of insurance investigators or something else that hides the true purpose of the visit," says Currie. "This may seem somewhat deceptive, but at this stage in the process, it's essential to maintain confidentiality. The more people who know a company is for sale, the less it's worth."

Phase 3: Negotiating

In phase three, prospective buyers stop kicking the tires and start talking money. Anyone seriously interested in the business will give you a "letter of intent" stating what they will pay for the company and outlining the terms of the payment and other major deal points. The letter of intent provides a starting point for the negotiations. It usually contains language allowing the acquirer to back out if certain conditions arise.

Never start serious negotiations until you obtain more than one letter of intent. The goal is to create an "auction" environment where several interested parties compete with each other for your business. According to Currie, an auction environment offers several important advantages:

- Allows you to play bidders against each other to raise the price
- Allows you to determine the market-driven value of the company
- Provides more flexibility during negotiations
- Gives you fallback options if things don't work out with your first choice

Once you have gathered several letters of intent, select the most promising buyer and announce that you have accepted their letter.

Phase 4: Closing

In this last phase, things *really* get serious. The buyer begins to conduct in-depth due diligence on your business while you also continue to learn as much as possible about them. During this time, both sides will engage in negotiating a "definitive purchase agreement," the legally binding document that will consummate the sale. This lengthy and complex document typically covers a wide range of issues, including but not limited to:

- Sale price and terms of payment
- Non-compete, consulting and/or employment agreements for the owner
- Severance agreements
- Closing and/or signing bonuses
- Earn-outs
- Equipment and real estate leases
- Licenses and royalties
- Stock value and distribution
- Lifestyle agreements
- Life and medical insurance
- Family employment

"Obviously, this phase requires heavy use of attorneys by both sides," says Currie. "To keep the deal moving forward, however, keep the lawyers on the sidelines as much as possible until you and the buyer have worked out the basics in plain English. Once each of you has a good understanding of the price, the terms and any other 'make or break' conditions, then it's time to bring in the lawyers. Clarify what you want to accomplish with the deal and tell them to find a way to make it happen. Lawyers tend to take adversarial positions, so the more you stay in control and make sure they are working toward resolution, the better your chances of closing the deal."

AVOIDING COSTLY MISTAKES

According to Currie, it doesn't take much to kill a deal. To increase your chances of a successful sale, avoid these common pitfalls:

- **Not being prepared.** In today's markets, just about everyone is an acquisition target. If you aren't prepared, you may make an easy target if a large company suddenly swoops in for the kill. At the same time, warns Currie, never get seduced into discussions unless you are committed to selling and have made the necessary preparations.

- **Breaches of confidentiality.** If word gets out that you have put your company on the market, the following can happen:
 - Employees may discuss the pending sale with people they shouldn't.
 - Morale can suffer. Employees may begin to look for new jobs.
 - Customer relationships can suffer from inconsistent service.
 - Competitors may tell customers that the business is being sold in the hopes of taking business away from you.

"Any of these situations will reduce the value of your business and its ability to continue performing as it has in the past," says Currie. "Keep everything confidential and conduct all discussions at a discreet off-site location."

- **Failure to check out the buyer.** You can waste a lot of time and do irreparable damage to the business by getting involved with potential buyers who aren't serious. Conduct as much due diligence on all potential buyers as they do on you.
- **Talking to only one buyer.** The quickest way to lower the value of a business is to limit your talks to one potential buyer. Conversely, the best way to determine the true value is through multiple buyers who each have a different reason for acquiring the business. "A single buyer always controls the transaction," says Currie. "Multiple buyers put you in the driver's seat."
- **Talking with competitors.** Beware of competitors that express an interest in acquisition. They may be trying to get you to reveal sensitive data such as margins, customer lists or other proprietary information. Competitors often represent legitimate buyers, but use extra caution when proceeding.
- **Underestimating the value of the business.** Most owners underestimate the value of their business because they base it on past performance rather than future potential. "Value differs according to the buyer," Currie points out. "Let the market – not a single buyer, appraisers or past data – determine your company's value."
- **Premature disclosure.** Never provide more than what is available to the general public until potential buyers sign a confidentiality agreement. Even then, do not disclose:
 - Specific customer or supplier information
 - Specific product margins
 - Trade secrets
 - Information about unprotected technologies
 - Corporate or marketing strategies
 - A detailed balance sheet

"The biggest and costliest mistake of all is the failure to use professionals," warns Currie. "Selling a business requires the advice of experienced experts at every step of the way. Plus, you still have a company to run. If you get too distracted from your duties, the business will suffer, thereby lowering its value in the eyes of potential buyers. Your best bet is to work with a reputable investment banker or merger and acquisition firm that is skilled in obtaining multiple buyers, experienced in transaction negotiations and capable of providing sound advice throughout the entire process."

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To discuss selling your business, please contact one of our Directors at
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